ALAN R. MULLER

The Rise of Regionalism

Core Company Strategies under the Second Wave of Integration

THE RISE OF REGIONALISM:

CORE COMPANY STRATEGIES UNDER THE SECOND WAVE OF INTEGRATION

De opkomst van regionalisering:
kernondernemingsstrategieën onder de tweede integratiegolf

Proefschrift

ter verkrijging van de graad van doctor aan de
Erasmus Universiteit Rotterdam
op gezag van de
Rector Magnificus
Prof.dr. S.W.J. Lamberts
en volgens besluit van het College voor Promoties.

De openbare verdediging zal plaatsvinden op
donderdag 3 juni 2004 om 13:30 uur

door
Alan René Muller
geboren te Niagara Falls, New York (USA)

Promotiecommissie

Promotor:
Prof.dr. R.J.M. van Tulder

Overige leden:
Prof.dr. S.J. Magala
Prof.dr. P.M.H.H. Matthyssens
Prof.dr. G.C.A. Junne

Erasmus Research Institute of Management (ERIM)
Rotterdam School of Management / Rotterdam School of Economics
Erasmus University Rotterdam

Internet: http://www.erim.eur.nl

ERIM Electronic Series Portal: http://hdl.handle.net/1765/1

ERIM Ph.D. Series Research in Management 38

ISBN 90–5892–062–3

© 2004, Alan Muller

All rights reserved. No part of this publication may be reproduced or transmitted in any form or by any means electronic or mechanical, including photocopying, recording, or by any information storage and retrieval system, without permission in writing from the author.

For Carter & Finn

ACKNOWLEDGEMENTS

The presumptuously thick book before you is the product of the long and winding road known as 'the PhD'. Fortunately I have learned that, despite the tendency to panic on occasion, if you stick to it and try to keep your wits about you, that road will lead to again and again to the same point of clarity while winding less and less each time around. In this book I have tried to stay true to my background in International Political Economy while bridging the gap to the field of Business and Strategy; in doing so I have had the advantage of moral, technical, practical and intellectual support from a large number of individuals, some of whom I, despite my best intentions, will undoubtedly fail to mention here.

First of all, thanks to my current colleages at the department of Business Society Management, who have contributed to giving me a laid-back work environment amidst the grey-suit hustle and bustle of a Business School, and who appear to see my American background not so much as a flaw, but rather as an asset! I am particularly grateful to my partners in crime Douglas van den Berghe and Arjen Mulder. Douglas 'broke the ice' for me my first two years in many ways, and provided a sounding board for ideas and insecurities while we shared a room and carpooled together. Arjen has been a source of inspiration and comic relief over the past few years and, thanks to the fact that our last names differ by only one letter and our rooms by only one number, we are fortunate enough to be regularly mistaken for one another. In this way we keep each other in check. Jeroen van Wijk deserves special mention for discretely and unassumingly offering guidance and showing an unabated interest in my progress, my person and my future.

Thanks also to the countless student assistants who throughout the years have made the SCOPE database possible, painstakingly entering data the old-fashioned way, putting up with the agonizingly slow learning curve of their daily supervisors (myself among them) and never getting sufficient credit for work done. This applies particularly to David Frans, whose contribution to SCOPE cannot be expressed in hours or in currency. It also applies to former student assistant and current Amsterdam PhD student in Fabienne Fortanier, who unwittingly and unintentionally continues to 'raise the bar' and force me to work and think harder.

Both within the world of SCOPE and without, I owe a great debt of gratitude to my PhD adviser Rob van Tulder, for his seemingly limitless ability to inspire, to come up with clever solutions, to juggle too many balls, and to give me just enough room – but not too much – to do my own thing. Our collaboration over the past few years has been extremely fluid, largely due to an unusual level of synergy and accord between our intellectual perspectives. My thanks also to my former thesis adviser at the University of Amsterdam, Gerd Junne, who in 1998 brought me into contact with his own erstwhile PhD student, just recently endowed with a professorship in Rotterdam. Additional mention goes to other academics who have been supportive of my research, such as Danny van den Bulcke and Rob Grosse.

A word of appreciation also goes to the 'boys' at Fource Consulting, who back in the day tried hard, but not too hard, to dissuade me from pursuing my dreams and introduced me to key concepts such as 'the mass marketing test tool' and 'the chasm'. The transition from 'the young and the eager' at Fource to a decidedly different atmosphere at Erasmus was infinitely greater than I anticipated.

Last but not least, my thanks to my parents, my sister and my friends for supporting me, encouraging me and expecting nothing less than the best I have to give. That support has also carried over across the Atlantic: established friendships on the 'American side' with people like Jesse Kerns and Casey Nault, which I know will last a lifetime, have been complemented by true friends on this side of the pond like Diederik van Hese and my two 'paranymphs', Mike van Akkooi and Moor de Leeuw.
During my period as a PhD student, however, the focus has shifted somewhat to center on my own little nuclear family through the birth of my two sons, Carter and Finn. They have made the challenge of completing my dissertation 'more or less on time' all the greater but all the more worth it. Of course I would not even have made it to writing these acknowledgements had it not been for Sofie, my rock in the stream, who had the wherewithal to egg me on, the love to believe in me and the patience to put up with my insecurities. Without her I would be a much lesser man.

Alan Muller

Haarlem, March 2004

TABLE OF CONTENTS

ACKNOWLEDGEMENTS i

ACRONYMS AND ABBREVIATIONS v

EXECUTIVE SUMMARY vii

1. INTRODUCTION 1

1.1 SUMMARY OF THE PROBLEM 1
1.2 RESEARCH QUESTIONS 3
1.3 RELEVANCE OF THE RESEARCH 5
1.4 STRUCTURE AND SCOPE OF THE STUDY 6

PART I: THEORETICAL BUILDING BLOCKS 7

2. INTEGRATION THEORY AND THE 'NEW REGIONALISM' 9

2.1 MAINSTREAM THEORIES OF REGIONAL INTEGRATION 11
2.2 THE ORIGINS OF REGIONALISM 17
2.3 MECHANISMS OF REGIONALISM 25
2.4 THE OUTCOMES OF REGIONALISM 30
2.5 MISSING LINKS 40

3. UNDERSTANDING THE DYNAMICS OF REGIONALISM 45

3.1 TOWARDS AN INTEGRATIVE, MACRO-MICRO APPROACH 45
3.2 THE MACRO/MICRO DYNAMICS OF REGIONALISM 51
3.3 REGULATION AND ECONOMIC RESTRUCTURING 58
3.4 THE CHOICE OF REGIONALISM STRATEGY 67
3.5 REGIONALISM AND THE SPATIAL ORGANIZATION OF ACTIVITY 75
3.6 PRELIMINARY CONCLUSIONS 82

4. CORE COMPANIES AND REGIONALISM STRATEGY 85

4.1 MAINSTREAM PERSPECTIVES ON INTERNATIONAL RESTRUCTURING 85
4.2 CORE COMPANIES AND BARGAINING RELATIONS 94
4.3 POSITIONING, ORGANIZATION AND BARGAINING RELATIONS 103
4.4 CORE COMPANY STRATEGIES AND REGIONALISM 115
4.5 ANTICIPATING THE DYNAMICS OF REGIONALISM 123

PART II: EMPIRICAL EXPLORATIONS 129

5. REGIONALISM'S 'SECOND WAVE' 131

5.1 THE SINGLE EUROPEAN MARKET (SEM) 132
5.2 THE NORTH AMERICAN FREE TRADE AGREEMENT (NAFTA) 141
5.3 OTHER MANIFESTATIONS OF REGIONALISM 150
5.4 UNDERSTANDING REGIONALISM IN A MULTILATERAL SYSTEM 155
5.5 MACRO-LEVEL CONCLUSIONS 163

6. INTERNATIONALIZATION AT 'T-MINUS': BASELINE 1990 165
6.1 SAMPLE SELECTION 165
6.2 DIMENSIONS FOR ANALYSIS 174
6.3 QUANTIFYING INTERNATIONAL STRATEGIES 179
6.4 NETWORK SPREAD AND ORGANIZATIONAL CHARACTERISTICS 191
6.5 STRATEGIES IN THE EU AND NAFTA 199
6.6 CONCLUSIONS 205

7. REALIZED REGIONALISM STRATEGIES OVER THE 1990s 207
7.1 REFLECTIONS OF REGIONALISM AS A STRATEGIC ISSUE 207
7.2 RESTRUCTURING ACROSS THE SAMPLE AS A WHOLE 210
7.3 EUROPEAN CORE COMPANY STRATEGIES 227
7.4 NORTH AMERICAN CORE COMPANY STRATEGIES 241
7.5 CONTRASTING EUROPEAN AND NORTH AMERICAN PATTERNS 254

8. SYNTHESIS: OPENNESS AND THE MACRO-MICRO LINK 257
8.1 OPENNESS IN EUROPEAN COMPETITIVE SPACE 257
8.2 OPENNESS IN NORTH AMERICAN COMPETITIVE SPACE 264
8.3 CONCLUSIONS ON THE AGGREGATE 270

9. CONCLUSIONS 273
9.1 MACRO- AND MICRO- DIMENSIONS OF INTERNATIONAL RESTRUCTURING 273
9.2 A GLOBALIZING OR REGIONALIZING WORLD? 277
9.3 THE POLITICAL ECONOMY OF REGIONALISM 281
9.4 POLICY RECOMMENDATIONS 284
9.5 LIMITATIONS AND DIRECTIONS FOR FUTURE RESEARCH 286

APPENDICES 289
APPENDIX I: THE SCOPE CORE200 289
APPENDIX II: SALES, ASSET AND SUBSIDIARY REPORTING IN THE SCOPE DATABASE 291
APPENDIX III: METHODS FOR MANIPULATING THE KEY VARIABLES 295

REFERENCES 301

SAMENVATTING (IN DUTCH) 319

BIOGRAPHY 325

ACRONYMS AND ABBREVIATIONS

AGE	Applied General Equilibrium
ASEAN	Association of Southeast Asian Nations
CAP	Common Agricultural Policy
CET	Common External Tariff
CGE	Computable General Equilibrium
CM	Common Market
CU	Customs Union
DSPs	Dispute Settlement Procedures
DUPs	Directly Unproductive Activities
DVI	Degree of Vertical Integration
EC	European Commission
EMU	Economic and Monetary Union
EPU	Economic and Political Union
ERT	European Round Table of Industrialists
EU	European Union
FDI	Foreign Direct Investment
FTA	Free Trade Area
FTAA	Free Trade Area of the Americas
GATT	General Agreement on Tariffs and Trade
HST	Hegemonic Stability Theory
IMF	International Monetary Fund
ISI	Import Substitution Industrialization
Mercosur	Mercado Común del Sur
MFN	Most Favored Nation
NAFTA	North American Free Trade Agreement
NEG	New Economic Geography
NTBs	Non-Tariff Barriers
OCA	Optimal Currency Area
PCU	Partial Customs Union
PLC	Product Life Cycle
PTA	Preferential Trade Agreement
RIA	Regional Integration Agreement
RTA	Regional Trade Agreement
SADC	Southern African Development Community
SEA	Single European Act
SEM	Single European Market
STT	Strategic Trade Theory
TCA	Transaction Cost Analysis
TNC	Transnational Corporation
TRIMs	Trade-Related Investment Measures
TRIPs	Trade-Related Intellectual Property Rights
VERs	Voluntary Export Restrictions
WTO	World Trade Organization

EXECUTIVE SUMMARY

Globalization, associated with economic liberalization and a commitment to free trade and investment, is one of the buzzwords of the 1990s. It is often associated with large multinational enterprises, which are assumed to become increasingly 'footloose' in their 'global' scope. This poses challenges for national policymakers, who have embarked on numerous large-scale supranational policy ventures in an attempt to channel the flow of economic activity. One of the more prominent forms of supra-national policymaking has been the tendency towards regional integration.

The resulting proliferation of regional integration agreements (RIAs) worldwide has drawn renewed attention to the phenomenon of regionalism as an object of research and theoretical analysis. The current 'second wave' of regional integration differs from earlier, import-substitution based strategies in numerous ways, adding multiple layers of complexity to the phenomenon. RIAs and their implications for welfare, economic activity and world trade are analyzed and interpreted in various ways, sometimes positive, sometimes negative, and sometimes as 'old news'. Are RIAs sustainable, or do they only lead to short term and unequally distributed gains? Are they a necessary step towards globalization, or an inevitable second-best option in a realist world? The confusion is not surprising given the lack of a comprehensive understanding of the problem.

Regional integration can be seen as a process of international restructuring, by which new institutions are built, driven and shaped by numerous stakeholders. Of these, firms and governments are arguably the most important. This observation, however, makes clear that the assessment of international restructuring processes like regional integration poses a level-of-analysis problem. National governments operate from a macro-level perspective, while firm strategy is formulated and executed largely from a micro-perspective (firm-specific stakeholders) and meso-perspective (competitors). As a result, strategic interests differ between perspectives, and at the same time they criss-cross and overlap across geographic space. Ultimately, governments and firms do not share the same strategic intent, nor do they perceive the same strategic reality.

As actors in a dynamic process, however, both firms and governments must have perceptions of each other's intent and reality. This may lead to misconceptions of the drivers of the strategic behavior which occurs in response to the formation of new institutions. The assumptions of strategic behavior are key because they largely determine the (expected) outcome of restructuring, particularly in terms of the spatial organization of economic activity and the rents which flow from this activity. Additionally, the dynamic and strategic aspects of international restructuring are related to the balance of power among the main actors. The role of 'core companies', a relatively select group of large firms which occupy 'core' positions in the economy and more often than not operate with one foot in the political process, is crucial to the dynamic. International restructuring is ultimately a small numbers game, with characteristics of oligopolistic competition at both the macro and the micro levels.

Traditional approaches to regional integration demonstrate shortcomings from this point of view, in descriptive, prescriptive and predictive analysis. Firstly, integration is often viewed in an overly simplistic fashion. In many cases RIAs are even exogenous to the analysis, or seen as a fully rational decision based solely on arguments of economic welfare. Regional integration, however, can be seen in the context of the dynamic interplay and competition *among* regional blocs (or other concentrations of economic power) as a

desirable strategic outcome in its own right ('regionalism'). Secondly, firms are rarely if at all considered explicitly in the analysis, neither as actors in the integration process itself, nor as individual players in a restructuring game with potentially 'sub-optimal' strategic interests. A comprehensive framework of regional integration must emphasize the role of both firms and governments as strategic actors in international restructuring, offer insight into the 'strategic repertoires' of both actors and analyze the outcomes of RIAs from this perspective.

A number of pilot studies notwithstanding, empirical research and analysis relating regional economic integration to internationalization strategies at the firm level has thus far been scarce. Theoretical work on multinational activity focuses almost exclusively on firm-specific determinants, neglecting environmental (locational) issues. Empirical work on multinational activity tends to focus on macro-level proxies of MNE activity, primarily focused on foreign direct investment (FDI). Others concentrate on a particular aspect of internationalization, such as R&D, subsidiary ownership patterns, networks or on a geographic area. Studies which do claim to take a firm-level view often do not in fact progress past the level of FDI, which is only a proxy for firm activity but does not take the firm as the unit of analysis. Such analysis does not, for instance, identify *who* is internationalizing, nor *why* they do so.

Others emphasize the macro-micro link but do not analyze RIAs as such, making only theoretical predictions of FDI in relation to existing RIAs. These studies may even emphasize the relevance of firm-level motivators (e.g. locational advantages and competitive position), but do not explore the possibilities of a broader framework with a set number of concrete variables, nor test their predictions empirically. At the single region, single-sector level, more in-depth work has been done on the automotive industry and Mercosur; on NAFTA), but this is rarely placed within a wider framework. The current study can be positioned in the context of a new research agenda which seeks to pay more attention to the spatial aspects of value-added activity within the context of company strategies.

The leading research question of the study focuses on Regional Integration as the outcome of strategic behavior on the part of firms and governments. It addresses in particular their mutual (mis)conceptions of the drivers and circumstances that shape each other's behavior, and thus how the resulting realized outcomes can differ from intended outcomes:

To what extent do firms organize their economic activity spatially in response to regional integration in ways that policymakers expect, and what does this say about the nature, significance and viability of regional integration as a vehicle of international restructuring?

This question is addressed by analyzing the policy motives behind various RIAs, of which the Single European Market (SEM) and North American Free Trade Agreement (NAFTA) are the most prominent. These motives are broken down into their intended impact on the organization of production, and to what extent the RIA is designed to be inwardly and outwardly 'open'. *Openness* refers to the effect integration has on shifting production 1) *within* the region by 'insider' firms (inside-in); 2) *to* the region by 'outsider' firms (outside-in); 3) *outside* the region by insider firms (inside-out), and finally 4) production shifts by outsider firms among third-party countries (outside-out).

The policy-designed ‘openness’ is first evaluated using trade and investment data to check whether the macro-level perceptions and expectations by national (and regional) policymakers played out in the regional economy. Trade data show that the SEM is relatively inward in orientation, with member countries trading far more amongst themselves than with the rest of the world. NAFTA countries, which have traditionally traded more with the rest of the world than with each other, are since 1997 also inward-oriented, trading more with each other. This stands in stark contrast with other regions such as the *Mercado Común del Sur* (Mercosur), Association of South East Asian Nations (ASEAN) and the Southern African Development Community (SADC), which are all overwhelmingly outward-oriented, and in general increasingly so.

Meanwhile, investment data reveal that European countries invest nearly as much in each other as they do in all other countries of the world combined. The countries of the NAFTA region, in contrast, are increasingly externally oriented as investors. The interpretation of increased inside-out openness must be made with caution, however, since the US dominates regional investment and Canada and Mexico remain very small investment targets compared to the rest of the (extra-regional) world. Additionally, in relation to their respective GDPs, inward investment stock from the US in Canada and Mexico has climbed dramatically over the second half of the 1990s.

At the macro level of analysis, decomposing trends to the level of individual firms is often largely hypothetical. This study has tried to fill this gap by analyzing the realized internationalization strategties and restructuring behavior of 122 of the world’s largest companies from Europe and North America. Taking their spatial organization of production in 1990 as a baseline, the study analyzes ‘strategy migrations’ both pre- and post-1995 to understand the dynamics of the second wave of regionalism. These ‘core companies’ are in the best position to know what the stakes of integration are and their internationalization strategies have a flagship function towards other economic actors. Moreover, regional integration in Europe and North America was largely facilitated through the lobby activity of many of these firms, both behind closed political doors as well as in the public media.

The research shows that regionalism has eclipsed the multilateral system as the ‘fast track’ for international economic restructuring. For Western core companies, regionalism has become the institutional framework of choice within which the struggle for preservation of their core positions is played out. This study differentiates between the different strategies firms can pursue within a range of ‘orientations’: domestic, regional (the home region), bi-regional (in practice the home region plus Europe for North American companies and vice-versa), and global (significant production in three or more regions). The data show that, in contrast to the ‘ideology’ of globalization, core company strategies and their strategic migrations over the 1990s have primarily taken place in the home region. Regionally oriented firms, for instance, which formed the largest orientational cluster in both regions in 1990, remained the largest group in 2001. The wave of mergers and acquisitions (M&As) in the second half of the 1990s also involved in particular regional core companies, which were relatively speaking three times as likely to be acquired by other core companies than firms with a different geographic orientation.

There has been considerable migration between orientational clusters and the average degree of internationalization (overall as well as extra-regional) rose significantly over the decade. Many of the firms which in 1990 were primarily domestic internationalized within their home region (although many US companies remained, or even became, domestic

over the decade), while regionally-oriented firms generally strengthened their regional positions. Other regional players, particularly in Europe, used integration at home to make the jump to establishing extra-regional positions in an attempt to establish footholds in 'non-captive' competitive spaces. The relatively small number of 'global' firms (only nine of the 122 core companies in the study) managed to maintain their global position but at the same time the group did not grow in size over the decade.

The internationalization trend was also to some extent contradicted by a considerable degree of *de*-internationalization. North American companies which were in the best position to exploit the opportunities of integration, such as US carmakers, retreated to a limited extent to their home region after 1995. Moreover, many bi-regional firms (both European and North American) struggled with the simultaneous gravitational pull of integration in both regions and either reduced their exposure in the second region or divested activities outside the two regions in order to concentrate on the bi-regional core. In this way a 'chasm' has emerged between regionally- and globally-oriented strategies. But even global firms that remained 'global' experienced de-internationalizion over the decade. Perhaps most crucially, the role of Europe in North American core company strategies and North America in European core company strategies declined in most cases relatively and in some cases absolutely as growth was sought *within* the home region and / or *outside* the second region.

The outcome is one of growing polarization between North American and European core companies, and consequently within an increasingly dyadic world economy. Regionalism seems thus to correspond better with the strategic intent of core companies than with that of governments. The tendency towards further regional expansion and consolidation (new EU members in Central and Eastern Europe; piecemeal extension of the NAFTA to the rest of the Americas) has therefore received strong support from core companies eager to extend their production networks. The Europe-wide cap on labor migration from the new members, however, is also a strong indication that in the upcoming 'Third Wave' of integration, policy-level strategic intent and core company strategic intent may continue to diverge.

1. INTRODUCTION

The recent proliferation of regional integration initiatives worldwide has drawn renewed attention to the phenomenon of regionalism as an object of research and theoretical analysis. Nearly all of the WTO's 144 members have concluded some form of Regional Integration Agreement (RIA) with other countries. In the period from 1948-1994, GATT contracting parties notified 108 RIAs relating to trade in goods, of which 38 in the five years ending in 1994. From the WTO's creation in 1995 through 1999, 67 additional RIAs were notified. The current 'second wave' of regional integration (Dent, 1997; De Melo *et al.*, 1993; Bhagwati, 1993; Laird, 1997) differs from earlier, import-substitution based strategies in numerous ways, adding multiple layers of complexity to the phenomenon. RIAs and their implications for welfare, economic activity and world trade are analyzed and interpreted in various ways, sometimes positive, sometimes negative, and sometimes 'old news'. Are RIAs a viable form of restructuring, or do they only lead to short term and unequally distributed gains? Are they a necessary step towards globalization, or an inevitable second-best option in a realist world? The confusion is not surprising given the lack of a comprehensive understanding of the problem.

1.1 Summary of the problem

One of the most pressing problems in economics, business and politics is where economic activity will locate in the future (Jovanovic, 2000). Globalization is one of the buzzwords of the 1990s, by which firms are assumed to become increasingly 'footloose' (Ohmae, 1990). Facilitated by developments in ICT and other technologies, firms are capitalizing on these opportunities to become global companies. This poses challenges for policymakers, who have embarked on numerous large-scale supranational policy ventures in an attempt to channel the flow of economic activity. One of the more prominent policy ventures of this sort has been the tendency towards regional integration.
Although science is largely preoccupied with the recent trend towards integration, it is by no means a new phenomenon. Integration goes in fact back to the time of the US colonies, (McGilvray, 1999), which were in effect sovereign policy spaces that chose to integrate their economic activity. In the 19th century numerous Bünde were formed among German states in unions that preceded the German nation-state, such as the Zollverein, the North German Tax Union and the Bavaria-Württemberg Customs Union (Mattli, 1999b). The phenomenon of integration is currently more pervasive and far-reaching than preceding generations of integration. Currently almost every country in the world is a member of a larger economic agreement between a number of countries and the bulk of the world's economic activity falls under the scope of one RIA or another.
Regional integration can be seen as a process of international restructuring, by which new institutions are built, driven and shaped by numerous stakeholders. Of these, firms and governments are the most important. This observation, however, makes clear that international restructuring processes like regional integration form a level of analysis problem. Governments operate from a macro-level perspective, while firm strategy is formulated and executed largely from a micro-perspective (firm-specific stakeholders) and meso-perspective (the competition). As a result, interests differ across levels of analysis, while at the same time these levels do not form a continuum in the real world. Rather, they

criss-cross and overlap, particularly across geographic space. Ultimately, government and firms do not share the same strategic intent, nor do they perceive the same strategic reality. As actors in a dynamic process, however, both firms and governments must have perceptions of the intent and reality of the other. This may lead to misconceptions of the drivers of the strategic behavior which occurs in response to the formation of new institutions, and in turn lays the groundwork for new institutional development. The assumptions of strategic behavior are key because they largely determine the (expected) outcome of restructuring, particularly in terms of the spatial organization of economic activity and the rents which flow from this activity. Additionally, the dynamic and strategic aspects of international restructuring are related to the balance of power among the main actors. International restructuring is ultimately a small numbers game, with characteristics of oligopolistic competition at both the macro and the micro levels.

Traditional approaches to regional integration demonstrate shortcomings from this point of view, in descriptive, prescriptive and predictive analysis. Firstly, integration is often viewed in an overly simplistic fashion. In many cases RIAs are exogenous to the analysis, or seen as a fully rational decision based solely on arguments of economic welfare. Regional integration, however, can be seen in the context of competition *among* regional blocs (or other concentrations of economic power) as a desirable strategic outcome in its own right ('regionalism'). Secondly, firms are rarely if at all considered explicitly in the analysis, neither as actors in the integration process itself, nor as individual players in a restructuring game with potentially 'sub-optimal' interests. A comprehensive framework of Regional integration must emphasize the role of firms and governments as strategic actors in international restructuring, offer insight into the 'strategic repertoires' of both actors and analyze regionalism outcomes from this perspective.

A number of pilot studies notwithstanding, empirical research and analysis relating regional economic integration to internationalization strategies at the firm level has thus far been scarce.[1] Theoretical work on multinational activity focuses almost exclusively on firm-specific determinants, neglecting environmental (locational) issues (Dunning, 1998). Empirical work on multinational activity tends to focus on macro-level proxies of MNE activity, primarily focused on FDI (Lipsey, 1999; Hagedoorn and Narula, 1996; Molle and Morsink, 1991). Others concentrate on a particular aspect of internationalization, such as R&D (Dunning and Narula, 1997); subsidiary ownership patterns (Ietto-Gillies, 1998), networks (Morsink, 1997) or on a geographic area (the Nordic school – Johansson and Vahlne, 1977) Several studies (e.g. Buckley *et al*., 1999) claim a firm-level analysis without progressing beyond the level of FDI, which is only a proxy for firm activity but does not take the firm as the unit of analysis.[2] Others, such as Ramstetter's (1996) analysis of Japanese firms, do emphasize the macro-micro link but do not analyze RIAs as such. Blomström and Kokko (1997) and Gestrin and Rugman (1994) make theoretical predictions of FDI in relation to existing RIAs (CUSFTA, Mercosur and NAFTA), and even emphasize the relevance of firm-level motivators (e.g. locational advantages and competitive position), but do not explore the possibilities of a broader framework with a set number of concrete variables, nor test their predictions empirically. At the single region, single-sector level, more in-depth work has been done (e.g. Neto, 1998, on the

---

[1] Some of the more notable exceptions are Robson 1993 at the theoretical level and Dunning 1997 at the empirical level.

[2] Such analysis does not, for instance, identify *who* is internationalizing, nor does it say anything about the *specific motivation* of the actor in question.

automotive industry and Mercosur; on NAFTA), but this is rarely placed within a wider framework. The current study can be positioned in the context of a new research agenda which seeks to pay more attention to the spatial aspects of value-added activity within the context of company strategies.

1.2 Research questions

The leading research question of the study focuses on regional integration as the outcome of strategic behavior on the part of firms and governments. It addresses in particular their mutual (mis)conceptions of the drivers and circumstances that shape each other's behavior, and thus how the resulting realized outcomes can differ from intended outcomes:

To what extent do firms organize their economic activity spatially in response to regional integration in ways that policymakers expect, and what does this say about the nature, significance and viability of regional integration as a vehicle of international restructuring?

This question comprises a number of subquestions:

1. How is regional integration addressed in the traditional literature?

The first step is to study the dominant body of literature on regional integration for what it reveals about the current understanding of the problem. What inherent assumptions are made, what frameworks are used, and what empirical results have been generated thus far? How convincing are they? Based on the analysis a number of criticisms, shortcomings and missing links are identified.

2. What is the nature and the outcome of dynamic firm-government interaction in regional integration as a process of international restructuring?

Based on the results of question 1, a strategic actor-based approach to the problem is developed. Assessing and understanding regional integration processes and outcomes involves a clear level-of-analysis problem. Regional integration is considered here as a process with an outcome determined by strategic behavior at both the macro and the micro level. Firm and policymaker strategic behavior has characteristics of oligopolistic competition in which particularly a small number of 'core' companies and policymaking entities struggle for dominant positioning relative to their competitors and to each other. Additionally, that behavior, and inevitably its outcome, is characterized by the mutual (mis)conceptions that exist at each level and which may lead to unexpected outcomes. Since the macro- and micro-domains of strategic behavior are interwoven through time and geographic space, outcomes are best measured in terms of dynamic shifts in the spatial organization of economic activity.

3. How can regional integration in its various forms be seen as a 'strategic repertoire' of policy behavior of national governments, i.e. as a typology of geopolitical ambitions?

This question addresses the motivations and drivers behind regional integration from a policy perspective (strategic intent) and the context in which regional integration is

adopted and implemented as a policy strategy (strategic reality). What factors and variables are relevant in this strategy? And what assumptions are made at the policy level (as reflected in theoretical and practical macro-models) concerning firm strategic behavior with respect to the chosen form of regional integration? These factors will be integrated into a 'strategic repertoire' of regional integration at the policy level.

4. What is the significance of regional integration for the spatial configuration and organizational structures of core companies?

Regional integration is generally seen as an exogenous shock instead of an outcome of firm strategic behavior. Therefore to address the same policy-level issues raised in question 3 at the micro level requires more in-depth analysis of relevant micro theories to distill components of firm-level strategy (proactive and reactive) that relate to regional integration as an outcome of institutional restructuring. To what extent is regional integration a strategic variable in micro theories? What assumptions as to the nature of firm drivers and motivation (strategic intent) do these theories contain, and which are relevant for an actor-based view of firm strategic behavior under regional integration? What, if anything, is missing? These factors will be integrated into a 'strategic repertoire' of regional integration at the firm level.

5. How can macro- and micro-strategic repertoires be compared and contrasted in a more comprehensive framework?

This question implies a confrontation between the macro and micro perspectives, thereby explicitly addressing the level of analysis problem. Which firm-strategic repertoire(s) is/are relevant for which RIA strategies? Do they rest on similar assumptions and mutual perceptions of strategic behavior? Can a typology be developed of 'macro/micro regionalism strategies', or are the differences in perception and expectation due to the level of analysis gap so great that the two levels are incompatible?

6. What strategic motives, and inherent assumptions of firm behavior, are evidenced in policy documents of the Single European Market (SEM) and North American Free Trade Agreement (NAFTA) as two prime examples of RIAs?

This and the following questions are empirical in nature. Examining the strategic intent of policymakers with respect to regional integration involves the selection of one or more RIAs for closer examination. Analyzing the world's leading core companies in terms of their home country affiliation and the most important RIAs governing the bulk of their activity leads directly to the SEM and NAFTA as the two most important RIAs for core companies in general. The SEM and NAFTA will be examined from a policymaker perspective to identify their positioning in the policy-strategic repertoire developed above, as well as the implicit or explicit assumptions of firm strategic behavior which they embody.

7. What realized restructuring behavior do core companies exhibit in their spatial configuration of activity and organizational structure under the SEM and NAFTA, respectively?

Question 7 addresses the outcomes of RIA strategies from the firm perspective (micro-reality) to determine whether firm strategic behavior reflects the strategic intent at the outset (as well as policymakers' expectations), and what the 'empirical results' have been.

8. Conclusions

Do these realities, and the realized strategic behavior of governments and core companies, collide over time? What does this mean for the future prospects of regionalism as a form of international restructuring? Can differences be traced to mutual misconceptions of macro and micro strategic intent? Or do firms, and/or policymakers, not do what they say? Are RIAs sustainable, or do they only lead to short term and unequally distributed gains? Are they a necessary step towards globalization, or an inevitable second-best option in a realist world?

1.3 Relevance of the research

In the wake of the 'Battles' of Seattle and Genoa, the stalemate in WTO-negotiations at Cancún and the tepid response of many Latin American countries to the Free Trade Area of the Americas (FTAA), international free trade agreements are increasingly a focus of social scrutiny. As the multilateral system grinds to a halt, the stakes of regionalism as an alternate route for international restructuring are automatically raised. The deepening of integration in Europe, currently at the stage of monetary integration but with a common European constitution in the offing, creates additional pressure on members and non-members to toe the line of free trade. Britain's decision to remain outside Europe's monetary union, for instance, has made it subject to fierce lobby pressure from large companies such as Rover. As the debate on the costs and benefits (and winners and losers) of large-scale international restructuring heats up, scepticism is fueled by apparent double standards on the issue of free trade. In most cases this involves trade conflicts between members of the world's two major RIAs, the European Single Market and North American Free Trade Agreement. The case of US tariffs on steel and Europe's refusals to allow imports of cheap Latin American bananas are two of the more notorious examples by which the reality of free trade does not live up to the rhetoric.

1.3.1 Scientific relevance

The literature on regional integration is rather unclear on the impact of firm strategies on regional integration and vice versa. Theoretical frameworks are largely missing, and empirical research has thus far been relatively fragmented. Furthermore, the literature often focuses on one particular region, makes hardly any difference between the national origins of firms, and very often does not surpass the level of individual case or sector studies. There is a big gap between micro studies of firm strategies and macro studies of regional integration. Often macro studies are based on highly stylized (or even unrealistic) premises of firm behavior (see the Cecchini Report on the impact of the SEM). Once we can establish the link between realized firm strategies and regional integration (both as an objective of lobbying strategies, as well as a contingent factor of firm strategy), more realistic policies can be designed and implemented in the area of regional integration. The assessment of the feasibility of various regional integration initiatives from the firm's perspective should make it possible to come to better predictions on the next step after

regional integration: further globalization or a world economy of relatively detached and closed regional economies. The role of transnational corporations as 'lynchpin' between these regions - supporting or frustrating the political aims - is of particular interest.

1.3.2 Managerial relevance

The research will improve the sophistication of International Management decision-making. It can be established for instance whether firms from different sectors have a different stake in regional integration, and what preexisting strategy means for post-integration strategies. Perspectives generated on the 'durability' of given strategies in a regional context will also provide substance for discussions on long-term strategy development.
The assessment of the dynamism of regionalism should enable managers to better handle the growing international institutional uncertainty that results from the different forms and trajectories of regionalism. What should managers anticipate as an exogenous function and what can they influence either directly (lobbying) or indirectly (through the choice of a particular strategic repertoire)? In addition, as regional integration deals with a renewed arrangement regarding the tradeoff between public and private goods, managers should be supported in a more rational assessment of the most appropriate form of regional integration.

1.3.3 Societal relevance

The claim of welfare maximization through regional economic and political integration will be further analyzed by looking at the impact of regional integration on firm strategies and to what extent these strategies have a positive effect on welfare through the creation of more or less sustainable and viable regions. Governments will gain insight in the effectiveness of their policy measures and the public will gain insight into the transparency of policymaking and its relationship to the strategic reality of companies. Insight will be gained on the relevance of home versus host firms in a regionalizing economy and the impact of regionalization on the multilateral trade and investment regime will be assessed.

1.4 Structure and scope of the study

The chapters largely follow the questions as formulated in section 1.2. The overarching structure of the study is based on a split between the theoretical and empirical components of the research project. Part I explores the problem from the relevant theoretical perspectives and in Part II the analysis is taken to the empirical level.
The study is explorative and descriptive in character. No model is developed, no hypotheses are tested, nor is a grand theory of regional integration formulated. Due to the nature of the problem as described in this introduction, a better understanding of the issues at hand is required to create a foundation for more fundamental research in the future. The current approach serves this purpose well by providing building blocks at the conceptual as well as methodological level, integrating various theoretical perspectives to create a better understanding and introducing new quantitative data and measurement tools with which to analyze the phenomenon of regionalism.

PART I:

THEORETICAL BUILDING BLOCKS

Many authors heralded the 1990s as the era of 'globalization', pointing to the ever-increasing scale of international commerce, information and capital flows and the decreasing significance of national borders in general (cf. Ohmae 1990, Porter 1990), embodied at the institutional level by the World Trade Organization's (WTO) multilateral trade regime. More recently, however, the globalization thesis has been countered by the paradigm of 'regionalism', according to which economic activity is conducted within economic blocs. From this perspective, macro-regions such as the EU or NAFTA are the dominant institutional framework within which economic and even political processes are structured and coordinated (Gilpin, 2001; Ethier, 1998; Dent, 1997; Bhagwati, 1993).

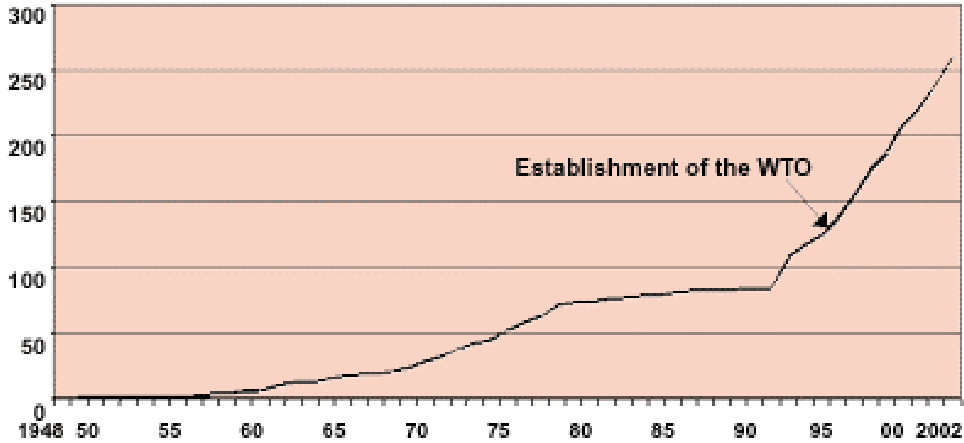
A multitude of schools of thought touch on the problem of regionalism and contribute to our understanding in many ways. However, their explanations, descriptions and prescriptions can be extremely diverse and incompatible. Moreover, the implicit or explicit theoretical understanding of the role of firms in the process and outcomes tends to be oversimplified. From the firm side, theory deals exhaustively with the drivers of firm behavior, ranging from cost issues to strategic, non-market factors yet has not given the regionalism phenomenon the attention it deserves. The first part of this study reviews the existing theoretical approaches at the macro and the micro levels, and develops a framework of understanding around which the relevant theoretical building blocks can be organized.

Chapter 2 has a dual function: 1) to review traditional theoretical approaches to regional integration and their empirical results in order to 2) identify the missing links of the analyses. Chapter 3 begins by proposing elements for an alternative framework by which to gain a more adequate understanding of the problem. The framework proposed introduces an actor-based approach to identify and integrate the motivations and strategic behavior of the key actors in regional integration processes. On the basis of this framework the real dynamism of integration can be explored and projections made for an assessment of the outcomes of regional integration. Subsequently regionalism as a strategy at the policy level is explored, dissecting the drivers, interests and behavior of governments with regard to regional integration. Pertinent theories will also be examined to gain an understanding of implicit and explicit macro-level perspectives on firm behavior, or policymakers' vision of micro-level strategic intent and strategic reality. Chapter 4 takes a firm-level perspective, addressing the relevance of regional integration for the strategic behavior of individual firms. Implicit and explicit drivers and strategic behavior will be distilled from various theories, and assumptions will be generated on the impact of regional integration on these drivers and behavior. Part I ends by reviewing the research questions in light of the theoretical constructs developed.

2. INTEGRATION THEORY AND THE 'NEW REGIONALISM'

The phenomenon of regional integration eludes precise definition (Dent, 1997), a fact lamented by early pioneers such as Viner (1950). To some, integration is described as 'regionalization', referring to the emergence of a regionally-oriented economic order, while others focus on 'regionalism', or purely political strategies for regional cooperation (Hettne and Söderbaum, 2000; Mattli, 1999a). Winters (1999) defines regionalism as 'any policy designed to reduce trade barriers between a subset of countries, regardless of whether those countries are actually contiguous or even close to each other' (p. 8). The tendency to refer to regions as 'trade blocs' overemphasizes the trade aspect of regionalism, and the word 'bloc' implies a defensive character (Cable and Henderson, 1994). For lack of better, most authors define a region in terms of geographic proximity (Mansfield and Milner, 1997). Cohen (1997), on the other hand, emphasizes a common currency as a basis for regionalism. Regionalism can refer loosely to the growing number of integrational links of varying intensity between individual nation-states (Dent, 1997), but is best exemplified by the rapidly rising number of new Regional Integration Agreements (RIAs) around the world over the 1990s (Atkinson, 1999; Ethier, 1998). In the period from 1948-1994, contracting parties to the General Agreement on Tariffs and Trade (GATT) reported a total of 108 RIAs relating to trade in goods, of which 38 in the five years ending in 1994. From the transformation in 1995 of the GATT into the World Trade Organization (WTO) up until 1999, 67 additional RIAs were notified (see Figure 2.1). By 2002 more than 250 RIAs had been reported and nearly all of the WTO's 144 members have concluded some form of RIA with other countries, and well over half of world trade is intra-RIA, with nearly all of the remainder inter-RIA (Ethier, 1998).

Figure 2.1: Number of RIAs reported to GATT/WTO, 1948-2000



Source: WTO Secretariat

The boom in RIAs over the 1990s has led some to speak of a 'second wave' of regional integration (Hettne and Söderbaum, 2000; Dent, 1997; De Melo *et al*., 1993; Bhagwati

1993). This new wave of regionalism differs from earlier, import-substitution based strategies (such as the Central American Common Market, or CACM, formed in 1960) in three important ways. Firstly, current RIAs are often formed between asymmetric partners, be it in terms of size (e.g. Luxembourg and Germany in the EU), development levels (e.g. US and Mexico in NAFTA) or both (Brazil and Paraguay in Mercosur). Secondly, they are in many cases a formalization of existing unilateral liberalization, in which reforms are 'locked in' or more easily sold to domestic stakeholders (De Melo *et al*. 1993). Thirdly, they are much more dynamic and complex, proceeding far beyond the issue of trade (Laird, 1997). Fourthly, they exhibit varying degrees of formal institutionalization, or legalization (McCall Smith, 2000).

Table 2.1: Selected examples of the 'first' and 'second' waves of regional integration

RIA	*Year*	*Members*	*Status*
First Wave			
Gran Colombia	1948	Colombia, Panama, Venezuela, Ecuador	
European Community (EC)	1958	Benelux, Germany, Italy, France	Succeeded by Single Market (1987) and European Union (1992)
Central American Common Market (CACM)	1960	Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua	Defunct in 1969, revived 1991.
European Free Trade Agreement (EFTA)	1960	Denmark, Switzerland, Liechtenstein, UK, Norway, Iceland, Finland, Austria, Sweden	Partial 'fusion' with EU after 1992
Latin American Free Trade Association (LAFTA)	1960	Mexico and all South American countries, except Guyana, French Guyana and Suriname	Partially implemented in the 1960s; not liberalized on schedule. Renewed attempt in 1990.
Association of South East Asian Nations (ASEAN)	1967	Indonesia, Malaysia, the Philippines, Singapore, Thailand, Brunei, Vietnam	Minimal liberalization achieved; rejuvenated in mid 1990s.
Southern African Customs Union (SACU)	1969	Botswana, Lesotho, South Africa, Swaziland and Namibia (from 1990)	Well integrated; common external tariff operational
Union Douanière et Economique de l'Afrique Centrale	1973	Cameroon, Central African Republic, Congo, Gabon, Chad, Equatorial Guinea	Little progress.
Caribbean Community (CARICOM)	1973	Antigua/Barbuda, Bahamas, Barbados, Belize, Dominica, Grenada, Guyana, Jamaica, Montserrat, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines, Trinidad and Tobago, Suriname	Little progress. New schedule outlined in 1990 establishing common external tariff.
Second Wave			
RIA	*Year*	*Members*	*Status*
Single European Market (SEM) / European Union (EU)	1987, 1992	Benelux, Germany, Italy, France, Spain, Greece, Portugal, UK, Denmark, Ireland, Austria, Finland and Sweden	Highly integrated.
North American Free Trade Agreement (NAFTA)	1989, 1994	Canada, US, Mexico	Successor of Canada US Free Trade Agreement (CUSFTA). Advanced trade liberalization.
Mercado Común del Sur (Mercosur)	1991	Brazil, Argentina, Paraguay, Uruguay (Chili and Bolivia associate members)	Initiated with promise but stagnating late 1990s
Southern African Development Community (SADC)	1992	Angola, Botswana, Congo, Lesotho, Malawi, Mauritius, Mozambique, Namibia, the Seychelles, South Africa, Swaziland, Tanzania, Zambia and Zimbabwe	Elements of policy coordination present; clear intention but as of yet limited real implementation of integrative measures
ASEAN Free Trade Agreement (AFTA)	1992	ASEAN (see above) plus Burma, Cambodia and Laos	In initial stages.
Free Trade Area of the Americas (FTAA)	200?	LAFTA and NAFTA	Under negotiation.

Source: Based partly on Mattli, 1999b: pp. 4 ff.

In the broad sense, governments have been cooperating in regional settings in the form of e.g. unions, leagues and commonwealths for hundreds of years, including e.g. the US colonies (McGilvray, 1999) and the German *Zollverein* (Customs Union) in 1816 (Mattli, 1999a). More recent efforts at regional integration dated from the 1960s, when many developing nations tried to profit from comparative advantages and larger markets while protecting their markets from global trade via import-substitution industrialization (ISI). This semi-autarkic form of 'free trade' was based primarily on tariff reductions limited to a small number of products, high rates of protection against third countries, and offered little scope for efficiency gains through the exploitation of scale economies (Laird, 1997). Whereas ISI strategies can be seen in the context of Cold War polarity, notions of Third-World dependency and fear of nationalist sentiments, the second wave adds additional layers of complexity to the phenomenon of regionalism.

Consequently, this 'New Regionalism' (Mansfield and Milner, 2000) has received renewed attention from academic circles. Despite an overwhelming and diverse body of literature, the 'hows and whys' remain poorly understood (Hettne and Söderbaum, 2000). Debates center on welfare gains and the implications of regionalism (especially the consequences for multilateralism), under what conditions states engage in Regional Integration Agreements (RIAs), and why and when integration takes the form that it does. Yet clear answers on the origins and implications of regional integration are lacking (Gilpin, 2001). Is regional integration nothing new and a non-issue? Does it lead to short-term or long-term gains, and for whom? Are RIAs simply accumulation regimes? Are regional blocs a step towards or away from 'globalization'? Is there such a thing as an optimal region, or configuration of regions, or is autarky the true natural state? Are regions sustainable? Are they even desirable?

Section 2.1 reviews the mainstream theories that deal with regional integration in general terms. Subsequent sections explores the explanations and assessments offered by theory in terms of the origins (section 2.2), shapes and forms of integration (section 2.3) and the consequences of integration (section 2.4). The concluding section, 2.5, focuses on the 'missing links' that need to be addressed systematically to provide a more sophisticated and holistic treatment of regionalism.

2.1 Mainstream theories of Regional Integration

To try and understand the key issues of regionalism, in particular given its increasing complexity, and address the questions posed above, requires an inventory of the mainstream theories that deal with the question of regional integration. Mainstream approaches to regional integration are traditionally categorized as based in economics or political science due to their distinctive respective assumptions and areas of focus. They can be classified as follows: 1) classical trade- and investment theories; 2) 'new' trade, political economy and economic geography theories; 3) functionalist 'bottom-up' political theories; and 4) statist 'top-down' political theories.

2.1.1 Classical trade- and investment theories

Traditional trade-oriented theories of regional integration draw largely on the seminal works of Viner (1950), Meade (1953) and Balassa (1961) and emphasize the 'static' effects of an RIA's internal and external barriers to trade. Viner's concepts of trade

creation and trade diversion under a Customs Union (CU) are fundamental to the analysis (Viner 1950). *Trade creation* refers to the increased tendency towards specialization (based on comparative advantage) and the resulting trade between CU members, which enhances welfare and increases income to both parties. Freeing trade within a given region can create trade by reducing prices, which in turn stimulates demand. *Trade diversion* describes the economic loss incurred when a common external tariff forces members to import a good from an RIA partner at higher cost than the good could be obtained on the world market. A high external tariff- or non-tariff barrier to trade, for instance, can divert trade to relatively higher-cost producers within the region and shut out the world low-cost producer behind the common tariff wall, creating a welfare loss to the region and to the world as a whole. Hence the merits of a given RIA are measured in terms of its ability to create more trade than it diverts, depending on relative tariff levels and shifts in trade flows.

Optimal currency area (OCA) theory, pioneered by Mundell (1961), examines the conditions under which it is economically efficient to create a currency union (or to fix exchange rates, cf. Mattli 1999). Changes (or stabilization) of the exchange rate affects flows of capital, markets of goods and markets of production factors. Factor mobility and integration of factor markets are included, because mobile factors are a prerequisite for an OCA. The higher the intensity of trade, the higher the benefits of a common currency (Yetati and Sturzenegger, 1999). In its initial form, OCA theory was highly apolitical, focusing only on the optimal size of such a currency area (Cohen, 1997). Gradually recognition grew that the OCA is an issue of sovereign states, which weigh the costs and benefits of surrendering their national currency autonomy. Krugman has emphasized that OCAs are a matter of macro-micro tradeoffs, because the consequence of giving up macroeconomic sovereignty is the gain of microeconomic efficiency (cited in Cohen, 1997).

More recently OCA theory has been expanded to include game-theoretic concepts, paying particular attention to bargaining and cooperation issues that arise in strategic settings characterized by asymmetric information and unequal distribution of economic capabilities among possible members of the union (Mattli, 1999a). From a strategic perspective, currencies are seen as a vehicle of competition between states or, in the case of an OCA, between areas or ‘regions’ (Cohen, 1997). Additionally, the role of private actors in reallocation processes has been recognized, making OCAs an issue not only of ‘political space’, but ‘economic space’ as well. Although OCA theory has been revived in the face of monetary union in Europe, as an empirical phenomenon it has remained relatively scarce, suggesting that perhaps the tradeoffs in favor of relinquishing currency sovereignty are not as positive as theory might suggest. In general OCA theory tends to downplay the significance of currencies as an element of national power and, as a consequence, loses a great deal of its theoretical value.

Increased recognition for the cross-border (productive) activities of in particular American MNEs (Hymer, 1976; Vernon, 1966) led subsequent studies of integration to focus on Foreign Direct Investment, or FDI. Approaches building on Kindleberger’s (1966) analysis of investment creation and investment diversion consider the ‘dynamic effects’ of an RIA (Clegg and Scott-Green, 1999; Belderbos, 1997; Gatz, 1997; Blomström and Kokko, 1997; Dunning, 1997; Gestrin and Rugman, 1994; Cantwell, 1993) which include greater competitive pressures (efficiency gains), technology transfer (directly and through spill-overs), access to superior management and production techniques, employment growth and

access to new capital (Dent, 1997). Such gains are considered 'dynamic' because they generate new activity and innovation, which in turn attracts new FDI, generating a new round of gains in a 'virtuous cycle of dynamic growth' (Connolly and Gunther, 1999).
The increased attention for dynamic effects and FDI has signaled implicit recognition for the role of companies in the process of effecting integration outcomes. According to Robson (1993), this recognition is also evidenced by the development of Industrial Organization frameworks (such as Dunning's OLI paradigm) which depict the horizontal or vertical (cross-border) integration of a firm's activities as an effort to internalize otherwise inefficiently operating markets, e.g. in the face of trade barriers (Dunning, 1992; Buckley and Casson, 1976), or exploit company-internal advantages such as technological know-how (Dunning 1997, Markusen 1995). In a similar vein, economic integration between countries could be seen as an attempt to 'internalize' international markets as well as the enhancement of region-internal competitive advantages. This suggests that motives for adopting the transnational mode of production also underlie the formation of regional blocs (Robson, 1993).

2.1.2 'New' trade theory, political economy and spatial economics

Strategic trade policy is a focus area of 'new' trade theory (Dixit and Grossman, 1986; Krugman, 1986; Helpman and Krugman, 1985; Krugman, 1990; Markusen, 1995; Baldwin, 1997). 'New' trade theory was developed in response to criticisms of classical trade theories' inability to explain in particular intra-industry trade and trade between developed countries with similar factor endowments. These additions to trade theory consider issues like oligopolistic competition, factor mobility, scale economies and barriers to entry (Markusen, 1995; Helpman and Krugman, 1989). Given the imperfect nature of markets, the assumption is that firms and governments, through strategic behavior, can improve the country's terms of trade through the use of 'optimal tariffs' (Gilpin, 2001). The optimal tariff argument is that a tariff improves a country's terms of trade if that country is large enough in world markets (exploitation of monopoly power), as well as through oligopolistic rents. The emphasis, however, on 'two / three firm, two country' models (Bowen *et al.*, 1998) means that models are oversimplified and particularly sensitive to variations in assumptions. Moreover, models differ on the assumption of either a 'horizontal' view of the firm, in which firms produce roughly the same goods in different countries, or a 'vertical' view, in which different stages of production are located in different countries – with very different results (Markusen and Maskus, 2001).
The recognition of potentially disparate gains from integration and the (theoretical) strategic use of integration for rent-seeking and the improvement of terms of trade has led some authors to model integration by endogenizing the political decision. Public choice theory models consider the choice between a Customs Union (CU) and a Free Trade Agreement (FTA) as a free rider problem in terms of lobbying (McLaren, 2000; Panagariya and Findlay, 1996). Then there is the Grossman-Helpman bidding equilibrium in which interest groups either donate to a politician's campaign fund or help to pay off campaign debts after the politician leaves office, and then politicians bargain on the basis off those payoffs. The diversity of interests in part determines which group (or the politician) gains the most. Approaches of this kind are innovative in that they incorporate domestic interests into international policy decisions, but rely heavily on classical economic arguments like rationality and full information availability.

The 'New Economic Geography' (NEG) pioneered by Helpman (1985) and Krugman (1990), and consolidated by Fujita *et al*. (1999), considers 'regionalization' outside of the policy sphere. NEG is not a theory of regional integration as such; rather, it implies that integration is a de facto endogenous outcome of the behavior of economic actors under specific market conditions. In doing so, NEG compensates for the shortcomings of traditional International Economics by addressing the question of why economic activity takes place in a given location and why it spreads. In addition, it abandons the realm of constant returns to scale, identical tastes and technologies and perfect competition in order to generate agglomerating effects. In the Dixit-Stiglitz stylized model of monopolistic competition presented in Fujita *et al.* (1999), traditional 'physics' of location (income, the price index, wage and transport costs) are all interrelated. Together they generate a number of handy agglomerating effects (love of variety, price index, and home market) and also leave room for the introduction of spreading effects (e.g. congestion). The inherent assumption of increasing returns means that market structure must be considered, as the former implies imperfect markets. At the same time, causation is cumulative (optimal location choice depends on what others do). This multiple-equilibria situation is characteristic of economies of scale; any resultant equilibrium will therefore depend on historical development.

Though not a theory of regional integration, NEG can be seen as suggestive of economic behavior when barriers to trade and investment fall, which arguably affects the perceived 'distance', and thus transport costs, between trading partners (Davis and Weinstein, 1999). The responsiveness of firms to trade and investment barriers has implications for policymaking as a vehicle for inducing agglomeration. Still, the policy aspect of regionalizing forces are neglected, the model itself is highly stylized and implausible, and empirics are inconclusive as to when a region is stable, growing, or shrinking. In addition, firms do not exhibit economically sub-optimal strategic behavior.

2.1.3 Functionalist theories of integration

Political science offers two closely related 'bottom-up' approaches, functionalism and neofunctionalism. The functionalist approach to integration entails functional cooperation at social and economic levels and is in this sense apolitical (Mattli, 1999). According to David Mitrany, one of the school's founding fathers, in a more 'natural' world order economic freedom would ensure that authority be linked to a specific activity, and not to a geographic area (Van der Pijl, 1992). Functionalism emphasizes security issues (a 'working peace') in integration, and sees states and governments as obstacles to what would otherwise be a bottom-up process for solving coordination problems. The approach entails both political and economic arguments: it suggests that if politicians step aside, rational economic behavior by actors in transnational society will generate irreversible, gradual steps towards a global division of labor. The underlying assumption is that politics is by its very nature conflict oriented and that politics is not the way to solve such issues.

Mitrany took a pragmatic, functional approach to integration ('the logic of ramification'), whose objective was to circumvent the polarity between total national sovereignty on the one hand and federalist tendencies towards supranational power structures on the other (Van der Pijl, 1992). Functional integration was not limited to geographic proximity and had no limits. Functionalism, while powerful in its concept of economic interdependencies,

was more a normative cry for an alternative means of achieving lasting peace than a theory of regional integration per se.

Neofunctionalism adds a utilitarian dimension to functionalism by addressing the practicalities of yielding sovereignty. Neofunctionalism embodies the notion that supranationality is the only method available to states to secure maximum welfare (Mattli, 1999). A first step needed to be taken, but then this would grow by itself into an integration process. Vehicles of integration are functional spillover, updating of common interests, and sub- and supranational group dynamics. Actors also have purpose (strategic intent) and function (unintentional outcomes that form a new strategic reality, allowing the actor to learn and adapt his purpose). So functionalist integration becomes a learning process (Van der Pijl, 1992). For Haas, the question was whether functionalist de facto integration would lead to the emergence of a new political community via 'federalism in stages' (ibid.).

A Functionalist approach would argue that such institutions emerge because there is a fundamental need for them (Braithwaite and Drahos, 2000), which rests in the reduction of policy complexity. One problem is that the consequence of creating the organization (reduction of complexity) in some sense becomes the explanation for its emergence. In any case it means governance change requires interventions at multiple levels (Cox, 1994).

2.1.4 Statist theories of integration

Intergovernmentalism, also called 'neorealism', assigns a central role to heads of states and their 'realist' motivations, emphasizing power-related variables. States interact in a decentralized, anarchic system, with bloc-formation between states as a solution to the security dilemma (Deutsch, in Gilpin, 2001). Central is the 'celebrated bargain', in which large and powerful states strike a deal and small states are paid off with side payments. Big states are more powerful than small states, and thus 'bargaining tends to converge towards the lowest common denominator of large state interests' (Moravscik, 1991). The security dilemma leads to bandwagon effects in which each region tries to increase its bargaining power relative to other regions (Gilpin, 2001). Cameron (1992) points out that neorealism contests the irreversible and inevitable nature of integration. Here states remain the most powerful actors and behave rationally, and are motivated by their desire to maintain and enhance their power relative to that of other states. The power-based argument for integration can be seen in the context of Servan-Schreiber's now-famous book 'The American Challenge', by which integration in Europe is seen as a defensive strategy of maintaining power relative to the US.

More recently the security dilemma has yielded to a more general view of solving common problems, particularly on the market. A more market-oriented perspective is embodied in the concept of an RIA as market-making between public 'demand' for integration and policymakers' 'supply' of integration (Mattli, 1999b). 'Regional institution-building may be viewed as an attempt to internalize externalities that cross borders within a group of countries. Externalities affecting cross-border trade and investment arise from economic and political uncertainty as well as a wide range of financial risks that market actors face when dealing with foreign firms and governments' (Mattli, 1999b: 3).

The apparent ability of the international community to build supranational cooperation despite the decline of US hegemony in the 1980s generated criticism of intergovernmentalist theories. Robert Keohane (1984), the main proponent of

neoinstitutionalism, saw international regimes as a way of dealing with collective action problems like market failures and transaction costs. Institutions can aid states in solving these problems together in the absence of a hegemon willing to incur a disproportionate share of the cost.

2.1.5 Structuring the mainstream literature

The theories discussed above all make significant contributions to our understanding of Regionalism (see Table 2.2). Yet they deal with the topic from a wide range of assumptions and points of departure. The level of analysis is overwhelmingly macro, the underlying logic (implicit or explicit) is very different, and key 'actors' are conceptualized differently, if at all. Drawing on this diversity to enhance our understanding of 'the New Regionalism' is a complex task.

Table 2.2: An overview of mainstream approaches to regional integration

	Conceptualz-zation of region	*Focus of inte-gration dynamic*	*Logic of integration*	*Level of analysis*	*Key 'actors'*	*Conceptualization of actors*
Customs union theory	Customs Union (CU)	trade shifts	trade creation, economic welfare	macro (supranational)	markets	the invisible hand
Optimal Currency Areas	Monetary Union / fixed exchange rates	trade and factor shifts	macroeconomic and factor market stability	macro (supranational)	markets	the invisible hand
FDI and Integration	Free Trade Area, Customs Union, Common Market	cross-border operations of firms	efficiency effects and dynamic growth	macro (supranational)	firms; governments	profit maximizing MNEs; policy realists
'New' Political Economy and Strategic Trade Theory	Free Trade Area, Customs Union	trade shifts	improve terms of trade, serve protectionist interests	macro (national)	policymakers and interest groups	rational, self-interested and welfare maximizing
New Economic Geography	Agglomeration of economic activity in geographic space	agglomerating versus spreading effects	cost minimization; endogenous to firm behavior	regional	firms	rational production processes; 'dots in space'
Functionalism	Not applicable	supranational institutions; interdependence of economic actors	peace through prosperity	macro (supranational)	economic actors	interdependent production processes
Neo-functionalism	European Coal and Steel Community	utilitarian behavior of actors	self-interest: welfare maximization	macro (supranational)	political and economic actors	self-interested utilitarian
Intergovern-mentalism	security bloc	the 'celebrated bargain'	increased national and regional security	macro (national)	heads of state	self-interested 'enlightened' leaders in pursuit of power
Neo-institutionalism	supranational institution	governments	solving collective action problem	macro (supranational)	states and supranational governance bodies	organizations for problem-solving

Approaches can be structured in different ways; predominant is the classification along economic and political lines but this is not very functional. Winters (1999) adopts a more complex (albeit weighted towards economics) taxonomy. In his account, approaches diverge in terms of objectives (welfare or other undefined 'political' considerations), interaction between countries (one-off or repeated), preferences and behavior (implicit or explicit), power dynamics (number of countries and number of trade blocs, and power

asymmetries between them), and inside and outside dynamics (members versus non-members). Since one objective of the current study is to understand better the hows and whys of regionalism, it makes sense to structure them in terms of causes and consequences, or origins and outcomes. In critiquing the mainstream literature from this perspective, we will touch upon the other matters, specifically the nature of interaction and the underlying assumptions of preferences and behavior.

2.2 The origins of Regionalism

What do mainstream theories offer in terms of the motivations behind regionalism strategies? Typologies of integrative impetus are revealing in terms of the assumed behavior and interests of economic and political actors. Authors generally distinguish between economics-induced and politically-induced integration, market-led and policy-led integration (OECD, 1996; Yoshida *et al*., 1994), or 'formal' versus 'informal' (*de facto*) integration (Dent, 1997). The distinction is rooted in the notion that economic actors prefer the removal of barriers while political actors prefer to build formal supranational institutions. Mattli (1999b) calls this supply-driven versus demand-driven integration. Other typologies emphasize the deterministic, functionalist character of integration ('natural' integration, cf. Bhagwati 1993), while still others focus on the strategic aspects ('defensive' integration, cf. Dent, 1997; or 'bandwagon regionalism', cf. Mansfield and Milner, 2000).
Such characterizations tend to reduce 'globalizing' and 'integrational' pressures to abstractions and downplay the role of politics and policymakers by giving regionalism a deterministic quality. In most RIAs the nation-state remains the primary level of decision-making, and recognition exists that transnational pressures are not likely to make the state obsolete (Lake, 1999). Since the rationale and arguments for RIAs are generally conceived at the national level, countries still form the primary unit of analysis. National policy preferences, and thus strategic choices, can be seen in terms of the domestic bargaining arena (the national level), or in terms of the interaction with other (potential) regional member states (the regional level).

2.2.1 Domestic demand for integration

Neofunctionalism is the first theory to address integration from the perspective of the integrative forces of economic actors. It has a deterministic character, suggesting that if there is a problem across borders, sub- and supranational actors will mobilize resources and the problem will be solved. Yet such an argument discounts the preferences, and even the very existence, of governments and lacks understanding of collective action problems. Neofunctionalism also suggests that supranationality is the way to maximize welfare, but no explanation is given of the relationship between integration and welfare maximization, and economic transactions remain mostly unexamined (Mattli, 1999a). It is not clear why the nation-state should be obsolete, and the implicit assumption that economic actors in their natural, 'undistorted' state will tend towards cooperation is based on a very neoliberal laissez-faire principle. Integration is seen as no more than a natural phenomenon without any real thought to the distributive consequences and the strategic interests of the parties involved. It lacks any notion of politics or 'power' (Caporaso and Keeler, 1995, cited in Cowles, 1995) and tends to ignore the role of events external to Europe (ibid.). Explicit

recognition of the significance of the policy level means that in particular functionalist approaches to the origins of regionalism are inadequate. Neofunctionalism does, however, focus on subnational actors and emphasize the role played by supranational institutions in catalyzing the process of integration.

In more recent literature, regionalism strategies can be seen as an attempt to 'supply' policy to meet the 'demand' that exists among domestic stakeholders, in particular big business. Mattli (1999b) draws on property rights theory and new institutional economics to describe the basis for domestic 'demand' for integration. In terms of the former, regionalism can be seen as an effort to internalize cross-border externalities which arise from uncertainty and risks faced by economic actors in dealing with foreign firms and governments (Mattli, 1999b). As cross border activity increases and economies become increasingly intertwined, the implicit costs of these externalities increases. Property rights theory addresses the role of institution-building as a mechanism for internalizing externalities when gains outweigh the costs. Creating property rights is then an allocative procedure that determines how gains are distributed. Changes to the environment, such as new technology and new economic patterns, can change the relative gains and costs of internalizing those externalities (Mattli, 1999b).

Similar arguments are given from a transaction cost perspective. Transaction costs are the costs of 'specifying, negotiating, monitoring and enforcing contracts that underlie exchange' (Williamson, 1975). Although transaction cost theory leans heavily on the role of technology in determining (potential) production processes and therefore cost, the broader idea that environmental change affects the costs underlying exchange is very applicable here. The assumption is that economic actors, in this case firms, experience some degree of uncertainty in dealings with other firms, which translates into relatively high transaction costs. Thus, as the environment changes, firms may lobby for institutional developments (e.g. protection) to mitigate that uncertainty and thereby reduce transaction costs. The function of the policymaker is then to supply integration. Supply conditions are those under which political leaders are willing to accommodate demand, which depends on the gains to the leaders themselves.

Unfortunately, as Helpman (1999) points out, the relevant models do not generate a coherent theory, primarily because there is no agreed-upon theory of domestic politics. As is the case with endogenous growth theory (e.g. Baldwin, 1985), this tends to be seen rather simplistically as the desire for re-election (political economy models), based on the assumption that political leaders value political power and will attempt to maintain that power. While the rationale may be true, such an argument assumes firstly that economic actors know what options are available to them, and what the cost-benefits are of these options. Secondly, it assumes that their individual cost-benefit calculations are independent of the behavior of other actors. Uncertainty is considered exogenous to the behavior of firms – there is no strategic behavior because rational economic action in free markets contributes to the welfare of all. Thirdly, it assumes these actors know how to influence governments to suit their ends, and that governments' primary interest is to supply policy as desired, when in fact governments themselves may have other strategic concerns at issue. The very transaction costs firms seek to reduce, for instance, may directly benefit the government (e.g., in the case of tariff revenues), such that the interests of 'supply' and 'demand' are actually opposed. Finally, it is given that the central policymaking decision is that between an FTA and a CU, i.e. *what* kind of region to form, whereas the option to

regionalize or not (the '*why*' of the region) generally remains unaddressed (cf. McLaren, 2000; Levy, 2000).

Much of the International Business (IB) literature (cf. Robson, 1993), on the other hand, highlights both the motives of political actors as well as the motives of firms in regional integration, but tends to assume by default that both types of actor are subject to identical problems and solutions. For instance, explaining both transnational production decisions and economic integration between countries as similar 'market internalization' decisions may be conceptually appealing but does not necessarily reflect the true strategic considerations of the actors involved. Additionally the tendency in IB to draw firm-level conclusions based on highly aggregated data reflects once again the bias of a one-dimensional approach. Even approaches which emphasize industry-level interests also 'neglect the fact that influencing trade policy primarily results from strategic decisions made by firms, not industries' (Rugman and Verbeke, 1991: 25).

2.2.2 Protectionism and strategic trade policy

At the same time, regionalism strategies can be part of a strategy to protect domestic industries from international competition while gaining the security of a larger market and growth potential. Although it is widely argued in economic theory as well as in policy circles that free trade (no tariffs) is far superior to tariffs and non-tariff barriers (NTBs), governments have in practice always attempted to control trade and deliberate agitation for true free trade has been scarce historically (Ethier, 1985). The logic of free trade has been argued from different perspectives over time. Whereas in the 1960s and 1970s it was analyzed in international political economy largely from a Marxist, dependency perspective, more recently even certain neoclassical economists have developed arguments in favor of protectionism. The dependency school advocated protectionism as part of a strategy of Import Substitution Industrialization (ISI), by which developing countries could be shielded from cheaper imported goods, thereby buying time to develop their own capabilities, strengths and scale. Although ISI strategies have generally been acknowledged as 'failures', more recently protectionist arguments have been made by economists in the form of 'Strategic Trade' policies. While ISI was particularly addressed to the situation of developing countries, Strategic Trade Theory (STT) focuses explicitly on high technology industries and intra-industry patterns of trade that characterize developed economies. This focus rests implicitly in the recognition that, given imperfect competition, some economic actors are potentially more attractive than others. Governments, in this sense, use protection to gain an advantage in global markets. There may of course also be non-economic reasons, such as ensuring domestic supply of strategically significant goods, e.g. military hardware, albeit at a higher cost. Additionally, it should be recognized that tariffs essentially represent a redistributive measure, redirecting a share of income *away* from market actors (and consumers) and *towards* governments. In this sense protectionism entails a recognition of benefits both to governments and firms as opposed to simply responding to domestic demand.

The incorporation of economics into politics (or vice versa) is an issue of political economy. Some theories, such as the political science variants of political economy and strategic trade policy, define economic arguments for political decisions behind protection. To economists, political economy refers to the 'endogenization' of political behavior into models, using economic techniques and behavioral assumptions of self-interest and

individual welfare maximization. This assumes that economic institutions are created to serve market efficiency, however, and that everything can be explained endogenously; i.e., as an attempt on the part of an actor to maximize his or her economic welfare (Gilpin, 2001).

Most of the possible explanations for the origins of regionalism come from political science theories. In political science variants of political economy, however, the nature of economic activity remains an open question. Interests, power and strategic behavior are distinguished at different levels of analysis. Regional integration, for instance, can be a question of benefits to individual consumers, promoting specific welfare goals or of maximizing national power.

Although the argument introduces strategic behavior on the part of both companies and governments, it has been criticized for lack of applicability to both real-world policy (Gilpin, 2001) and firm-strategy situations (Waverman, 1991). Criticizing protectionism as a policy strategy does not do away with the fact that pressure from domestic interest groups may continue to exist, despite the supposedly self-evident flaws in protectionist logic. The counter-arguments of free trade are often lost on those groups which stand to lose most by changing the status quo, and their political pressure can sometimes be irresistible. Trade creation, in the words of Albert Hirschman, can be a political liability. Gilpin (2001) argues that the relevance of the 'new trade' theory for trade policy has been exaggerated by those too willing to misuse economics for rent-seeking purposes, and as Samuelson once suggested, 'one must be careful when businessmen parrot economic theory' (Waverman, 1991: 60). 'Misuse', however, is subjective in the sense that protectionism represents real political and economic interests that can be powerful forces in shaping policy, regardless of the strengths and weaknesses of their arguments.

2.2.3 Pressuring domestic stakeholders

The assumption is often made that in international policymaking, governments only act in the expressed interest of their constituents. Domestic pressure groups, meaning societal or economic stakeholders, are considered to have the implicit ability to unseat governments through their voting behavior. Many theories, therefore, fail to take into account the possibility that governments might enact policies contrary to those interests. In fact, government interests and thus policy preferences may be determined by factors other than domestic pressure groups, and structural reforms may be a response to such external pressures as powerful economic partners, regional hegemons or supranational institutions like the IMF. In such cases, regionalism strategies can be used to leverage governmental power against domestic interest groups in a more adversarial relationship. From a neoinstitutional perspective, economic interdependence 'multiplies the opportunities for altering domestic coalitions (and thus policy outcomes) … in effect creating political entanglements across national boundaries (Putnam, 1993; cited in Cameron and Tomlin, 2000: 22).

Regionalism can be an attempt by government to shape comparative advantages and influence the capabilities of the national economy (Jovanovic, 2001). Regionalism can also serve to formalize, or 'lock in', liberal reforms (e.g., in the case of Mexico) by forming 'commitment institutions' (Mattli, 1999b: 170) which are at least to some extent controlled by outside forces. Often this is looked at the international political level, particularly as a coordination dilemma. Yet the commitment to regionalism can also be a strategy for

pressuring local stakeholders to adhere to policy by increasing the 'weight' of policy in general, as a way of 'tying the government's own hands'. Some of the National Business Systems literature (see Whitley, 1999; Hollingsworth and Boyer, 1996; Lazonick and O'Sullivan, 1996; Whitley and Kristensen, 1996) tends to look at regional integration in this way, considering policy as implemented from above and analyzing its impact in terms of the pressure it places on local stakeholders.

Regionalism strategies can be part of an effort to shift power relations with domestic stakeholders, such as union leaders and big business. The government, for example, may feel that companies are not contributing successfully enough to national competitiveness and force them to restructure through exposure to additional competition. Tension may exist between interests in policy space and competitive space, particularly if government is not solidly rooted in civil society. Additionally, democratic mechanisms may also not be effective enough to 'perfectly' transmit domestic interests. This may particularly apply to developing countries in the context of 'North-South' integration, where the ideological gap between stakeholders is great. Political economy models (cf. Winters, 1999) argue that the effectiveness of political pressure, and hence the incentive to undertake lobby activities, by predominantly nationally-organized interest groups declines under integration. The resultant distribution of political decision-making power towards governments may in itself be a reason to engage in integration.

Policy initiatives may be described as an attempt to mold competitive space in such a way that it is better compatible with policy spaces. A perspective based on policy initiatives as leading, however, does assume for its part some kind of information asymmetry, and that stakeholders (or, most relevant for our analysis, core companies) might not fully understand the stakes of the game, the range of options available to them, nor have a clear understanding of what the government's interests are. The alarming diversity in *ex ante* predictions and *ex post* analysis of even the two most high-profile regions in the world, the EU and NAFTA, shows that the stakes in the real world are far from clearly defined.

2.2.4 Collective action problems

The newer institutionalist theories emphasize regionalism as an example of international cooperation in solving collective action problems (Gilpin, 2001), rooted at least to some extent in frustration with the apparent inability of multilateral process to solve such problems. Institutionalist theories generally seek collective action problems in the realm of welfare problems, such as the stability of the international monetary system (Mattli, 1999b). Regionalism can be explained as a response to a number of problems particularly in terms of transaction costs and diseconomies of scale at the multilateral level (Haggard, 1997). These are regional-level market failures that lead to an inability to couple regional supply and demand, with extra-regional supply and demand 'leakage' as a result. This line of thinking emphasizes regionalism as a powerful tool to enhance competitiveness in each of the constituent nations as well as a way to promote interest and investment in the region by the international community. By creating competitive advantage on a regional scale, countries could draw in additional sources of growth and free up intra-regional resources through scale economies. The injection of additional resources and competitive pressures would create innovative pressures that would ultimately allow the region to compete on the basis of superior technology. From a more realist perspective, explanations for regionalism

are traditionally sought in the context of security as the fixed, unitary goal of states (Cohen, 1997).
The central issue in collective action problems is the provision of public goods. The critically received Hegemonic Stability Theory (HST) argues that a stable international order can only be maintained in the presence of a hegemonic power willing to incur the costs of providing certain 'global' public goods (Gilpin, 2001). Most recently, the United States is portrayed as having fulfilled this role, while Great Britain was the hegemonic power in the 19th century. Whereas proponents of Hegemonic Stability Theory (HST) look to a strong, dominant state to provide such goods, the question remains as to who provides the public goods in the absence of a hegemon. The cost-benefit analysis of providing public goods, and the risk of free-riders, can have the characteristics of a Prisoner's Dilemma (Mattli, 1999b) in which the gains from steps taken depend on the behavior of other actors. On the other hand, some argue that the power vacuum in the hegemon's absence signifies a removal of a key obstacle to enhanced economic cooperation. In this sense the origins of the second wave of regionalism can be seen in the shift to a multipolar, tripolar or even bipolar structure as a consequence of declining American hegemony (Hettne and Söderbaum, 2000). The absence of a hegemon thus necessitates collective action but at the same time impedes multilateralism. Multilateral failure (e.g. the OECD's abandoned initiative for a Multilateral Agreement on Investment, the MAI, and the troubles surrounding the WTO) may also be symptomatic of the limits of real state policy in the face of UN weakness; regionalism, therefore, may be the most logical response.
However, even though regionalism can be seen as the solution to a number of collective action problems, it creates new ones of its own. An additional problem is that Prisoner's Dilemmas fail to consider the distributive element of trade bargaining, i.e. the distribution of power among players and the relative gains, losses and risks incurred by each. Haggard looks at integration not from the PD perspective, but more from the perspective of trade bargaining as a distributive game between small and large players. Haggard argues that, despite theoretical predictions suggesting greater potential gains from integration as the number of members increases, a larger number of members also increases the likelihood of divergent preferences and reduces the likelihood of striking a bargain (Haggard, 1997). It is therefore theoretically possible that there is a critical mass to collective action problems such that governments do not expect more parties to be beneficial; in other words, there may be an 'optimal number' of member states (Padoan, 1997). Preferences can become too diverse, such that it becomes ineffective and the ability of individual governments to affect outcomes diminishes.
Although neoinstitutional theory has been influential in our understanding of regional institutions, it has not generated a theory of economic and political integration (Gilpin, 2001). In addition, Sandholtz (1999) has criticized the neoinstitutionalist approach on the grounds that there is little evidence that such cooperative agreements actually reduce transaction costs, in part because such agreements are most likely to occur where transaction costs are already low, and notoriously difficult to measure. Additionally, the intergovernmentalist emphasis on this bargain in isolation ignores the context of integration (Mattli, 1999). There is too much emphasis on the enlightened leader, when the term of office is likely to expire far before the fruits of integration can be plucked. In addition, there is overreliance on the presumption that a large state (hegemon) will play a key role, incurring extra costs in guaranteeing stability. Lastly, regime theory suffers from a lack of true empirical research on the actual functioning of specific regimes, which

makes it difficult to determine whether or not regimes actually make a difference in the conduct of international affairs (Gilpin, 2001).

2.2.5 'Defensible' multilateralism

A variant to the argument of an optimal number of members is that of regionalism as an attempt to create 'defensible' multilateral institutions in which a higher degree of national sovereignty is retained. Economic linkages in general increase security (Ohmae, 1990), but there still exists a trade-off between economic growth and autonomy. Regionalism strategies may be undertaken simply as a way of maintaining some control over the organization of economic activity in what Braithwaite and Drahos (2000) call 'paradoxes of sovereignty'. If a supranational institution is too large, individual members run the risk of losing control over policy and may opt for a more 'manageable' degree of sovereignty cession. This rationale is particularly used in cases of developing or otherwise economically weak or vulnerable countries fearful of multilateral liberalization and its consequences, or in the case of expansion of a pre-existing region (a kind of path dependency) which Winters (1993) calls 'managed liberalism' (p. 212). The defensible multilateralism approach can also be a flanking strategy for countries when wider multilateralism stalls. The United States may provide the classic example of such an approach, where bilateralism and regionalism are employed when multilateralism stalls, or when the multilateral path requires too great a concession of sovereignty, which is an issue of particular sensitivity for the US. As a conceptual argument 'defensible multilateralism' is attractive but it does not show how to define the right size, or what the criteria are for such a collective action problem that the number of interested parties would have an optimum. This depends on the perceived degree of common vision, or shared preferences in a particular area of policymaking.

One of the problems, however, with regionalism as a strategy to solve collective action problems is that it seems to rest on the assumption that the international economy is something exogenous, while it is in fact a product of the behavior of strategic actors, including nation-states. Additionally, while the problem of collective action, public goods and free riding demonstrates the strategic game elements of international cooperation, a true theory of cooperation must also address the more fundamental question of policy preferences and the capabilities of the relevant actors. Key dimensions here are discrimination between insiders and outsiders (regionalism as the provision of 'club' goods), and distributive issues between potential members.

2.2.6 Maximization of national power

Idealist perspectives of integration view the recently growing impetus to integrate as a strategic complement, meaning that the more countries that integrate, the greater the gains are for all members (Krugman, 1991b). Such arguments, however, downplay the distributive effects of trade policies by ignoring self-interest (Gilpin, 2001). Bhagwati and Baldwin were among the first to recognize that governments often fail to enact the policies identified in theory (Feenstra *et al.*, 1996). Their political economy trade models made trade policy endogenous, recognizing that governments are not benign welfare-maximizing entities but rather pursue other, potentially sub-optimal objectives (Panagariya and Findlay, 1996). However, the value of these trade models for policymaking has been

overemphasized (Waverman, 1991), in part due to the lack of diversity in national interests in which they incorporate (Gilpin, 2001).

Nonetheless, governments are certainly very much motivated by national self-interest and can use regional platforms to defend those interests. The 'competition state' (Cerny, 1999) continues to use its power to channel economic activity to suit its national interests, including receipt of a favorable share of the gains from international economic activities (Helmut Schmidt's competition for the 'world product': Gilpin, 2001) and preservation of national autonomy. 'One should see [regionalism] as an integral part of a national competitiveness strategy, one that complements domestic economic reforms designed to improve productivity and promote the ability of local industries to compete more effectively against foreign suppliers at home and in the world markets' (Hufbauer and Schott, 1993: 116).

This line of thinking presents the collective nature of regionalism as a vehicle for achieving nationally defined goals with a relative minimum of compromise (Gilpin, 2001) as opposed to the provision of supranational 'public goods'. Regional integration is a way to increase national wealth, and therefore power, in global terms (rent-seeking). Such theories emphasize the fact that RIAs embody conflicting interests, and that reality is a global arena of sometimes conflicting policy domains. The concept that regionalism is inherently discriminatory can, in this sense, refer to the distribution of gains from integration among members, not just relative to third parties or 'outsiders' (Haggard, 1997). Prakash and Hart (1999) argue that regionalism, in addition to being an *expression* of inter-state rivalry, may in fact even *promote* inter-state rivalry, largely through the enhancement of systemic power (cf. Strange, 1994).

Rivalry between nations and supranational institution-building is not just a question of the risk of defection and the creation of commitment institutions to catalyze the process, in whose absence RIAs could only be stable based on repeat-play, issue-linkage and reputation (Mattli, 1999b). Since some countries have more market power than others (Cameron and Tomlin, 2002), some will attempt to maximize their own interests or welfare, just as firms do under oligopoly and market power conditions. The assumption that there is little or no communal interest leads to an asymmetric game in which equilibrium outcomes can be reached with one or more players unhappy, described by Lisa Martin as a 'suasion' game (cited in Haggard, 1997: 31). RIAs thus create a coordination dilemma (Mattli, 1999b) where policy preferences are not predefined but depend on the behavior of others. Equilibria are self-enforcing, but hard to come by. In a model by Gatsios and Karp (1995), on the other hand, 'weaker' states can actually profit by allowing a more 'aggressive' member state to lead negotiations. This quasi-hegemonic approach argues that a single powerful state, with the resources of an entire union at its disposal, can achieve more in international negotiations than individual states, or than regions with collectively defined, pluralist preferences.

The impetus to integrate may beget a kind of 'bandwagon dynamism' that Mattli (1999b) calls 'the first integrative response'. This involves an effort by third-party countries to get into an existing RIA ('club' membership) and therefore circumvent some of the initial costs. This behavior is a form of me-too strategy, but as a 'retaliatory response' to minimize potential losses or being 'locked out' of the gains from integration (oligopolistic reaction) instead of as a 'strategic complement' (Head, 1998). The maximization of national power or self-interest is also reflected in the desire to engage in regionalism simply because other nations do so. The region may welcome such efforts, since the

attraction of new members (like Austria and Sweden in the case of the EU) will enhance its international bargaining power. Whether the aspiring candidate's strategy is successful depends *inter alia* on the costs of membership, and what the potential candidate has to offer. The price of joining a successful region, Mattli (1999b) argues, can be prohibitively high such that the 'me-too' strategy may require the initialization of a new region as opposed to accession to a preexisting one.

2.3 Mechanisms of Regionalism

What is the purpose of policymakers in shaping the institutions that govern economic behavior, and what are the means, or 'mechanisms' (Braithwaite and Drahos 2000) by which they do so? Realist theories try to explain international behavior in terms of interests and power alone but are insufficient because they ignore institutions (Keohane, 1984). Supranational institution-building rests on international cooperation, defined by Keohane (1984: p. 51) as the adjustment of actors' behavior to suit the actual or anticipated preferences of others, through a process of policy coordination. The current 'fad' of globalization might suggest that international cooperation is a deterministic, natural process, but in fact it is always contextual; history has always born witness to a 'seesaw' between nationalism and internationalism, both in terms of intellectual trends as well as real political ones (Wallerstein, 1974).
What tools are available to policymakers in building supranational institutions, and how are they implemented? From a policy point of view, institutions are formal matters consolidated through policy intervention, particularly those affecting the (re)distribution of resources. A number of factors are important in developing institutions: the degree of pluralism, type of public policy development process, definition of the public interest, and the influence of lobby techniques (Wartick and Wood, 1998). Braithwaite and Drahos (2000) emphasize a range of 'push' and 'pull' mechanisms such as military or economic coercion, systems of reward, reciprocal adjustment and non-reciprocal coordination. Braithwaite and Drahos (2000) argue that coercion ('the stick') is more important than reward ('the carrot'). What are the restrictions, such as national stakeholder configurations and multilateral legislation, to the use of such policies? The following subsections address the primary areas of policy mechanisms governments use to build the institutions which influence the organization of economic activity: trade and investment policy, competition and industrial policy, monetary and fiscal policy, international agreements and treaties, and dispute settlement mechanisms. These policy tools are considered primarily from the point of view of the (national) government as the predominant policymaking institution. What do these mechanisms suggest about the behavior of market actors?

2.3.1 Trade and investment policy

Barriers to trade and investment consist of mechanical barriers to the flow of goods and production factors into (and sometimes out) of a given policy space. While tariffs, or taxes, remain the most common barrier to the flow of goods, 'non-tariff barriers' (NTBs) such as voluntary export requirements (VERs), quotas, trade-related investment measures (TRIMs), trade-related aspects of intellectual property rights (TRIPs) are increasingly common. Tariffs and NTBs affect the price of goods to consumers either by raising the real cost price or by determining their relative scarcity. The flow of production factors, in

particular capital, is regulated through TRIMs such as minority interest restrictions, national treatment of foreign investors, rules of origin (local content requirements), export-performance requirements, production mandates, mandatory technology transfer requirements and local-manufacturing requirements (Graham, 1997). Investment measures essentially determine the ability of foreign investors to invest, or artificially alter the relative attractiveness of the target country.

The logic of trade and investment policy is still predominantly shaped by neo-classical approaches to economics. National policy preferences, rooted in Ricardian comparative and absolute advantage, are ultimately determined by relative production factor endowments. Countries with different factor endowments will produce most efficiently by producing goods for export using factors in which the country has a relative advantage, and importing products from abroad that use factors compared to its trading partners. On the basis of this theory, the production factor used relatively intensively in the production of export goods will gain under free trade, whereas production factors used intensively in import-competing production will gain most from protection. In terms of interests, these production factors were at first translated abstractly into 'capitalists' and 'workers', but are looked at in an applied sense from a sectoral point of view. Gains and losses are primarily investigated on the basis of one-off policy interventions (considering only the response of 'market' actors and not taking possible policy retaliation into account).

There do exist limitations to national policy sovereignty in such matters. Whereas tariffs and quotas are essentially measures enacted by the importing country, they can conflict with international agreements. Voluntary export requirements (VERs), on the other hand, are concessions sometimes ceded by and sometimes forced upon the exporting country that sneakily circumvent such agreements (Schwartz, 1994). This only works if the importing country is powerful enough to threaten sanctions. Although membership in the WTO implies adherence to the principles of free trade, the reality is somewhat more flexible. Countries use trade and investment measures when they are beneficial, and decry any attempt to limit free trade if such measures could be harmful. Given the predominance of free-market ideology, government intervention in trade and investment is considered undesirable.

Regional integration is generally seen in this way, depending on the degree to which the RIA creates or diverts trade and investment. Although regional integration is formally frowned upon in the WTO, provisions under the Enabling Clause and Article XXIV (and Article XIX) of the GATT create 'loopholes' through which RIAs become practically viable. Article XXIV, which contains the main provisions concerning Territorial Application, Frontier Traffic, Customs Unions and Free Trade Areas, requires that a CU or FTA cover substantially all trade, and that for those items which are included, 'duties and other restrictive regulations are [to be] eliminated', i.e. that there is to be a 100 per cent reduction in tariffs and other barriers, a preferential rate other than zero is not contemplated. Article XXIV is 'notoriously lax' (Haggard, 1997: 29). The Enabling Clause, formally known as the Tokyo Round Decision on "Differential and More Favourable Treatment, Reciprocity and Fuller Participation of Developing Countries" (Laird, 1997), formally allows for the creation of preferential trading arrangements between developing countries, as long as they do not raise barriers or create 'undue' difficulties for third parties. One of the main criticisms of Article XXIV is that it does not subject RIAs to meaningful review even in respect to its own defined criteria since the outcome of the review process is controlled by the RIA member states (Abbott, 1999).

2.3.2 Monetary and fiscal policy

Monetary and fiscal policy are the primary elements of macroeconomic policy. Strictly speaking, monetary policy is the means by which the government controls the money supply and, as any other good under laws of supply and demand, thus determines its relative value. The money supply is controlled through interest rates, which affect the investment behavior and production decisions of firms. In the international context, the relative value of a currency determines the exchange rate. Exchange rate volatility affects cross-border capital flows as well as the value and flow of trade through inflation, devaluation, exchange rate pegs. Exchange rate fluctuations can lead to hysteresis, by which the circumstances around trade and investment decisions change over time and automatically alter the strategic relevance of the decision (Bowen *et al*., 1998).

Fiscal policy affects e.g. government spending and interest payments on government debt, but its central mechanism is taxes. Taxes affect growth by stimulating labor supply, consumer spending and investment. Fiscal policy has an increasingly important international dimension given the increase in cross-border capital flows. For certain countries, fiscal policy can form the foundation of a competitive advantage through tax exemptions, rebates and generally low taxes, particularly on corporate activity (so-called ‘tax havens’).

It has been argued in the theory of optimal currency areas (OCA; see section 2.1.1) that supranational coordination of macroeconomic policies (primarily by means of a fixed exchange rate) can improve employment and price stability. Recent history has seen two major attempts to manage macroeconomic policies supranationally. The first, the gold standard which existed prior to World War One, failed when the international distribution of gold stocks failed to reflect international flows of trade in goods (Schwartz, 1994). The second, known as the Bretton Woods agreements, were essentially designed to reconcile aggregate demand and the balance of trade, while minimizing the risk of international policy conflict (Ethier, 1985). The adjustable peg system served to keep exchange rates within a manageable bandwidth. Only the European Union has seriously exploited the possibility of monetary union (aside from numerous examples of ‘pegging’ and currency unions in West Africa and the Caribbean) within the context of regional integration.

There are certain limitations to the sovereignty of nations when it comes to policies designed to alter capital flows. On the one hand, countries which are members of the International Monetary Fund are required to observe certain guidelines on e.g. inflation, debt ratios and central bank accountability, and on the other hand, capital can only be controlled through policy interventions up to a point. The choice of the Argentine government, for instance, to maintain the peso’s peg to the dollar through 2001, despite its glaring overvaluation, became ultimately an untenable strategy which was punished on international capital markets.

2.3.3 Industrial and competition policy

Industrial and competition policy are concerned less with the aggregate economy and more with the behavior of individual consumers, firms and markets. As such its theoretical roots can be found primarily in the field of microeconomics. Industrial policies are intended to manage the decline of old industries and the rise of new ones, while competition policies are aimed at maintaining the intensity of competition (Johnson and Turner, 2000). By

changing market structure, government can e.g. stimulate inter-firm rivalry (Dunning's business-analytic approach). Rivalry and competitiveness are the goals of competition and industrial policies. Policies may be in the area of deregulation (to remove legal impediments to competition), as well as a wide range of social, regional and R&D programs (to correct market failures; cf. McDonald and Potton, 1994). An example is the requirement of government approval of mergers and acquisitions (see Graham, 1997).

McDonald and Potton (1994) distinguish three approaches to industrial and competition policy, based on different rationales and assumptions of behavior: market-based policy, interventionalist policy and selective intervention. The first, also called negative intervention, entails a minimalist approach to regulation, based on the assumption that markets are best able to allocate resources. The second, also known as positive intervention, is based on the assumption that the government has a constructive role to play in the elimination of market failures. Selective intervention entails the strategic use of policy to aid rising industries, based on the assumption that the competitive environment is imperfect. In that case limited government intervention can help firms gain a competitive advantage without permanently and extensively altering the market structure.

The use of industrial and competition policy can differ widely across countries (and regions). Although there is an increasing tendency towards market-based policy orientation, intervention remains widespread as governments (despite the rhetoric of liberalization and deregulation) continue to protect or subsidize declining industries (McDonald and Potton, 1994). In the case of regional integration, national governments generally have to make concessions to partner countries in order to harmonize policies, which in turn alter the incentives and behavior of economic actors.

Industrial and competition policies also encompass a host of policy terrains both positive (more government intervention) and negative (less government intervention). Governments may agree to set up structural funds to aid in the development of weaker (micro)regions within member countries or agree on other subsidy structures (such as the CAP, or Common Agricultural Policy, in the European Union). Other structural market interventions can be found in the realm of e.g. labor market policies to help buffer the restructuring adjustment costs of integration as economic activity shifts.

2.3.4 International agreements and supranational policy

While governments largely have exclusive jurisdiction over policymaking in the aforementioned areas, such policies are sometimes insufficient for the achievement of certain goals. Additionally, they are indiscriminate to the extent that all economic actors are exposed to the same regulations and operating environment. Yet some strategic goals necessitate international cooperation in the form of bilateral or multilateral agreements. Agreements can cover a wide range of mutually important issues, such as the use of each other's infrastructure, mail or telecommunications services, transport, and environmental and social issues.

Axelrod and Keohane identify reciprocity as one of the most important concepts in describing the emergence of cooperation (Braithwaite and Drahos, 2000). Reciprocal adjustment, when actor interests drive them to an agreement on the same rule or convergence of rules (Braithwaite and Drahos, 2000). 'Non-reciprocal coordination is when actors back each others interests because they think they will get something out of it later, in different terms. Yet there is often a lack of differentiation between the interests

and goals of different actors (Underhill, 1994). In neoclassical institutionalism, the origin and functioning of all types of institutions are explained as the result of the maximizing behavior of rational individuals (Gilpin, 2001). Regime theory takes a more 'idealist' approach to a non-hegemonial world, expecting convergence of expectations and behavior. Governments are not single-purpose unitary actors, often they are ambivalent and international agreements usually consist of a mixture of cooperative and conflictual behavior (Underhill, 1994). Interests must not be over-generalized.

Agreement does not, therefore, erase differences in interests among members. In fact it generally entails some kind of mutual concessions made by all parties, although some may concede more than others. In terms of specific issues, some members may share the majority view, or a common interest, while others are forced to yield. The 'equilibrium' achieved on any given issue can change as new countries become party to an agreement, or as other circumstances change. This makes e.g. controlling membership expansion a mechanism of regionalism strategies.

2.3.5 Dispute settlement procedures, sanctions and screens

Inherent to policy decisions, and the international agreements that substantiate those decisions, is the assumption that parties to such agreements will adhere to their stipulations. This is, however, not always the case given that the agreement is not a direct representation of each member country's individual interests. Supranational institution-building creates a compliance problem (Gilpin, 2001) generally addressed by dispute settlement procedures (DSPs). DSPs are central to the performance of international institutions (Mansfield and Milner, 1997). In regional integration terms, DSPs represent the degree of 'legalization' of a RIA (McCall Smith, 2000). This is a more explicitly political dimension which implies that countries, in their international cooperation efforts, are primarily in pursuit of their own interests. Depending on the exigencies of the moment, it may or may not be in a given government's interest to adhere to an agreement. Theory looks at trade policy as a repeated game, where each country weighs the short term gain of deviating from its commitment against the longer-term loss implied by the future imposition of punishing trigger strategies (i.e., adopted based on other actors' past actions) by other countries (Ethier, 2001). Yet deviation has little value these days, where punishment can be immediate: in other words, the short term keeps getting shorter. Treaties can also be considered incomplete contracts (Ethier, 2001), which require the threat of DSPs and sanctions to hold up.

Dispute settlement procedures are in theory designed to limit unilateral action in breach of an agreement by means of the threat of sanctions. For international trade, for instance, the GATT/WTO provide the central provisions for disputes. Additionally, agreements or policies are often discriminate, and not aimed at all potential actors. In institutional theory these are known as screens. Generally parties choose to negotiate rather than punish (ibid.). Ethier also argues that disputes are inherently bilateral and not multilateral. Under regionalism, however, the region itself can act, as in the case of the European Union. The European Commission is a party in 87 of the 244 disputes presented before the WTO from 1995 through 2001. Disputes can be a political and an economic tool for achieving specific goals. Alongside motives of 'leveling the playing field' and 'fighting unfair trade' exist motives such as 'retaliation'. Here is where reciprocity comes in (see above). Prusa and Skeath (2001) found in researching the motives behind the use of DSPs (in this case

antidumping filings) considerable evidence of strategic motives for the use of antidumping beyond simple economic grievances.
DSPs are not simply a matter of governments challenging other governments and their policy actions. They are particularly aimed at the behavior of firms operating under the jurisdiction of, or legally seated in, a country party to the agreement. In the case of trade disputes, governments are held accountable for the actions of the firm(s) accused of breaching the agreement. DSPs are thus a key example of how governments and business actors interact in institutional development.

2.4 The outcomes of regionalism

Just as with typologies of regionalism origins, typologies of outcomes are quite revealing. Although the variety of outcome-related typologies is much greater than for origin-related typologies, the distinction between economic and political outcomes remains the most pervasive (see Table 2.3). Theories of economic outcomes are considerably more disputed and ideologically laden than theories of political outcomes, in part because economic outcomes are more difficult to identify and isolate.

Table 2.3: Types of regionalism outcomes

Typology dimensions	*Primary operationalizations*	*Examples*
type of RIA	♦ # of policy areas (scope of cooperation)	♦ Hufbauer and Schott, 1994; Jovanovic, 1992; Balassa, 1961
positive vs. negative	♦ supranational institution-building vs. dismantling of national barriers to trade	♦ Mansfield and Milner, 1997
depth of integration	♦ degree to which policy sovereignty is ceded in a particular area of policymaking	♦ Cable and Henderson, 1994
intensity of cooperation	♦ independent regional bodies, regional ministers	♦ cf. Ten Napel, 1998
openness	♦ openness to new membership, share of extra-regional trade in total trade	♦ Bergsten, 1997; Bhagwati 1993
trade-creating vs. trade diverting	♦ whether regional producers are lowest-cost producers in terms of world prices	♦ Viner, 1950; see Winters, 1993 and 1999
investment-creating vs. investment-diverting	♦ whether RIA distorts investment market through e.g. 'tariff-jumping' FDI	♦ Kindleberger, 1966
economic asymmetry	♦ relative development levels	♦ McCall Smith, 2000; McGilvray, 2000
degree of legalization	♦ dispute settlement mechanisms	♦ Abbot, 1999; McCall Smith, 2000
political asymmetry	♦ strength in international negotiations; ♦ locus and number of 'core' countries and pluralist tendencies in decisionmaking	♦ Cameron and Tomlin, 2002; ♦ Van Tulder and Audet, forthcoming

2.4.1 Political outcomes of regionalism

Much of the literature addresses political and institutional outcomes, emphasizing various dimensions which have thus far only rarely generated true taxonomies. Some authors distinguish between *deep* and *shallow* integration, referring to the extent of policy coordination, which is to some degree a question of subsidiarity (Cable and Henderson, 1994). Deep means that not only trade is liberalized formally, but also NTBs are addressed, like government procurement procedures, a clear surrender of sovereignty, liberalization

beyond 'request and offer', and institutionalized DSPs. It should be noted that deep integration is not the same as harmonization. The harmonization of e.g. environmental standards in the case of NAFTA, for example, may be de facto a barrier to trade since they artificially eliminate cost disparities (ibid.). A similar axis is negative versus positive integration, which essentially distinguishes between the simple dismantling of barriers (supposedly in the interest of economic actors) and the actual building up of institutions ('positive integration') assumed to be primarily in the interest of political actors.

The emphasis has been overwhelmingly on policy-level outcomes, described typically in terms of the 'scope' of integration, or the number and type of policy areas subject to joint coordination. This may involve *i*) barriers to trade and services; *ii*) restrictions on investment; *iii*) labor movement; *iv*) harmonization of monetary and fiscal policies; and *v*) the construction of supranational institutions (Hufbauer and Schott, 1994). Whereas the classical distinction in RIAs has traditionally been between free trade areas (FTAs) and customs unions (CUs), the increasing complexity of regional integration can be demonstrated simply by reviewing successive attempts over the years to categorize RIAs. Balassa, in his classic work *The Theory of Economic Integration* (1961), was the first to expand on a conceptual range of integration forms: the free trade area (FTA), the customs union (CU), the common market (CM), the economic union (EU) and total economic integration (EI). It is only recently that variations have been made to Balassa's framework, primarily focused on the latter two forms (cf. McDonald and Dearden, 1994; Hoekman and Kostecki, 1995), largely a result of developments in the European Union. Dent (1997) redefined these as on the one hand economic and monetary union (EMU) and on the other economic and political union (EPU). Jovanovic (1992) introduced an additional two forms, the preferential trading agreement (PTA) and partial customs union (PCU), which essentially are variations on the FTA and CU, respectively. A brief overview of the various forms and their key characteristics follows in Table 2.4.

Less ideologically colored typologies are e.g. those of a region's 'intensity', referring to the frequency of cooperation and the measures taken to ensure joint character, such as the number of ministers with a relevant portfolio and the frequency with which they meet. Similar categorizations can be made by size (number of members), level of economic development and terms of compliance, or durability. Compliance and durability are often described as the degree of legalization of a region (McCall Smith, 2000). Cameron and Tomlin (2002) take a more power-based perspective by addressing power asymmetries in regions, i.e. the extent to which a region's members are more or less equal in terms of bargaining power. Typologies deal primarily with institutional arrangements, while the real political significance of Regionalism remains largely speculative. On the one hand there is a debate on the nature of growth regimes; on the other hand on the hollowing out of the state or even regulation in general, where unregulated gaps are left to the exploitation of market actors. Other debates center on the possibility of convergence between national institutional structures, and the impact of that convergence on national business systems or modes of accumulation (Whitley and Kristensen, 1996). Even political economy models (Winters, 1999 cites Levy, 1996 and Bhagwati and Panagariya, 1996) address the ability of a government to respond to e.g. exogenous shocks before and after integration. Ultimately this is simply a question of policy sovereignty. The more extensive the range of policy cooperation and/or harmonization, the less liberty a given government has to dictate policy and the less 'sovereign' that government will be.

Table 2.4: Main forms of regional integration and their characteristics

Form of RIA	*Main characteristics*
PTA Preferential trade agreement	♦ Mutual preferential treatment of signatories ♦ Lower customs duties/tariffs than for non-signatories
PCU Partial customs union	♦ Application of a common external tariff (CET) against non-signatories ♦ Intra-union customs duties/tariffs remain unchanged
FTA Free trade area	♦ Removal of most customs duties/tariffs between signatories ♦ Individual national tariff systems towards non-signatories remain in place ♦ Local content measures (rules of origin) apply
CU Customs union	♦ Removal of most customs duties/tariffs between signatories ♦ Application of a CET for non-signatories
CM Common market	♦ Removal of most customs duties/tariffs between signatories ♦ Application of a CET against non-signatories ♦ Free movement of factors of production (capital, goods, services and labor) between signatories
EMU Economic and monetary union	♦ Removal of most customs duties/tariffs between signatories ♦ Application of a CET against non-signatories ♦ Free movement of factors of production (capital, goods, services and labor) between signatories ♦ Introduction of common currency
EPU Economic and political union	♦ Removal of most customs duties/tariffs between signatories ♦ Application of a CET against non-signatories ♦ Free movement of factors of production (capital, goods, services and labor) ♦ Introduction of common currency ♦ Common policies on broader issues, e.g. foreign policy and defense

Regionalism should not only be seen from the perspective of individual nation-states and cooperation/competition within a single region; the region itself can be seen as a collective actor on a global stage of national and supranational institutions. The example was already given of the European Commission (EC) as an actor in international trade disputes on behalf of its member states. A proactive regional-level approach to trade disputes may in fact be ‘protectionism with a polite face’, where companies employ the regional government to keep their competitors on the defensive instead of shielding themselves behind outright protectionist measures. Others worry that institutionalized regional-level governments may create a ‘democratic deficit’. Hirst and Thompson (1999) argue, on the other hand, that regions can bolster democracy and that the EU will not become a ‘nation-state writ large’ (p. 231). But most argue in the context of the federal versus confederal state: are policymakers democrats, or are they pragmatists trying to get the best deal?

From a neoinstitutional perspective (Keohane, 1984), it could be argued that regionalism, as a surrogate for hegemony, facilitates the formation of even larger, supra-regional regimes. Regional integration may lead to a ‘domino effect’ (Baldwin, 1993), or ‘bandwagon dynamism’ (Van Tulder and Audet, 2004). This is Mattli’s (1999b) ‘second integrative response’, namely that the fear of being locked out of integration gains precipitates me-too strategies in the form of competing regionalist initiatives. The ‘second integrative response, much like a realist interpretation of the ‘second wave’ of regionalism, assumes that bloc-formation would lead to parallel integration efforts (in essence a realist, intergovernmentalist approach). Winters (1999), however, suggests that an intergovernmental union would tend towards protectionism, because an intergovernmental

construction is by its nature bureaucratic. In Winters' argument, drawn on Messerlin (1983) and Scharpf (1988), incentives for bureaucrats tend towards protectionism and the institutional construction inherently draws influence away from voters and towards official preferences for administrative convenience.

Realist, power-based analyses of regional integration reiterate the importance of historical development: any given RIA cannot be studied in isolation, as it is a strategic response to a given global context. Sandholtz *et al*. (1992) take a similar geo-economic approach in which the strategic interrelationship between the Triad is emphasized, heralded by the end of the cold war and the decline of US hegemony. International competitiveness is therefore seen as a security issue, with regionalism forming the basis for 'peaceful' economic competition instead of military competition. Cable and Henderson (1994), however, caution that tension between trade blocs may simply be the result of different standards and rules, and not necessarily strategic competition. This word of caution only serves to underscore the fact that the mainstream theories reviewed in Section 2.1 are largely inadequate in their understanding of the political significance of regionalism, for they fail to explain the wide range of forms and outcomes of integration (Mattli, 1999b).

2.4.2 Economic outcomes of regionalism

The significance and meaning of economic outcomes, or the impact of RIAs on economic activity, also remain shrouded in relative mystery. In traditional economics and International Business approaches, the focus is on the trade- and investment-creating and diverting characteristics of an RIA. The rationale is rooted in the concept of the larger market, which can reduce the market power of individual firms and has in turn a positive effect on competition and innovation, reducing prices and generating welfare benefits to consumers. These are growth regimes based on productivity growth, achieved through either a division of labor, technology, comparative advantage and specialization. Yet classical economics approaches in particular introduce a simplistic understanding of economic activity as basic production processes without a geographic component. Economic activity is defined by assumptions of 'markets' and the 'invisible hand'. Location of production is static, a matter only of factor endowments, with additional markets serviced by exports.

Returning to the list of types of RIA, the economic impact anticipated per type (Table 2.5) can be examined. The 'shallowest' form of integration, the preferential trade agreement (PTA), is expected to lead to increased trade between partners. Tariff barrier reduction translates directly into lower costs for consumers, as the costs of transporting goods across borders falls. As demand increases in response to lower cost, production increases. A reallocation of resources follows along lines of comparative advantage, and increased specialization through the potential for scale economies, which allows costs to fall again (a virtuous cycle of growth). Assumes elastic demand, markets clear, uniform tastes, small number of products etc. In addition, goods can be purchased from a larger number of sources as suppliers in other countries become attractive through the reduction of cross-border transport costs. This reduces the monopoly power of a country's firms in that country's markets (McDonald, 1994).

Table 2.5: Expected economic outcomes by form of integration

Form of RIA	*Theoretical outcome*
PTA Preferential trade agreement	♦ Increased intra-regional trade through specialization (comparative advantage) ♦ Trade and growth driven by lower cost (price mechanism) ♦ Potential for scale ♦ Increase in possible sources of supply reduces monopoly power within member countries
PCU Partial customs union	♦ Stimulation of intra-regional industry through protection of a regional market
FTA Free trade area	♦ Increased intra-regional trade through specialization (comparative advantage) ♦ Trade and growth driven by lower cost (price mechanism) ♦ Potential for scale ♦ Increase in possible sources of supply reduces monopoly power within member countries ♦ Local content measures (rules of origin) prevent exploitation of 'cheapest' member country as export platform
CU Customs union	♦ Increased (overall) trade in goods among members ♦ Potential for scale ♦ Increase in possible sources of supply reduces monopoly power within member countries ♦ Common external tariff (CET) to prevent export-platform exploitation of lowest-tariff member by non-signatories
CM Common market	♦ Increased intra-regional trade through specialization (comparative advantage) ♦ Common external tariff (CET) to prevent export-platform exploitation of lowest-tariff member by non-signatories ♦ Optimal regional resource allocation through free movement of production factors (markets clear) ♦ Regional division of labor based on specialization ♦ Regional coupling of supply and demand; prevention of supply and demand leakage ♦ Growth through specialization, scale economies, productivity gains
EMU Economic and monetary union	♦ Price stability ♦ Increased employment ♦ Increased market transparency ♦ Stronger currency and extra-regional competitive position
EPU Economic and political union	♦ All of the above, plus growth effects related to e.g. increased consumer confidence due to higher degree of political stability

The effects of a partial customs union (PCU) depend on the outcome of the CET. If the CET is higher than the (weighted average) pre-CET tariff barrier, then the PCU is essentially an attempt to stimulate sources of growth within the region by offering them uniform protection behind the CET. Free trade areas (FTAs) have the same basis as the PTA, but introduce local content measures. Local content requirements, or rules of origin, stipulate that a certain percentage of the value of a given good must be added within the borders of the FTA in order for that good to be exempted from excise. Rules of origin thus ensure that the increase in trade generated by the FTA is based on goods produced in the member countries, leading to growth *within* the region, and prevent non-member states from exploiting the lowest-tariff (or lowest production cost) member country as an export platform for serving the larger market of the FTA. Rules of origin prevent demand from 'leaking' outside the region. Rules of origin are particularly interesting when production costs differ widely across members. Depending on how the value is measured, relatively more work has to be conducted in a cheap labor member than in a high-production cost member before the percentage is reached (if measured in US dollars, relatively more added

value must be concentrated in Mexico to get the same percentage as would be obtained by concentrating relatively less in the US). Rules of origin must always be considered in the context of tariff reductions, because usually it is a give and take.

The Customs Union (CU) introduces the Common External Tariff (CET) which to a certain extent is a substitute for the rules of origin found under an FTA. Since goods produced outside the region have no possibility for preferential access via the market with the lowest external tariff, no member can be exploited as an export platform. The Common Market (CM) is distinguished on the basis of the free movement of production factors (goods, capital, and labor). In this way supply and demand for goods, capital and labor can be met at the regional level, which prevents ‘leakage’ of supply and demand (regional goods being sold extra-regionally and extra-regional goods being imported, respectively). Economic and Monetary Union (EMU) creates new prospects for growth through the introduction of a common currency, which, much like OCA theory, reduces uncertainty in investment, encourages reallocation of factors, and drives prices down through transparency. Economic and Political Union (EPU) is a hypothetical case in which transaction costs and thus uncertainty are reduced by the institutionalization and stabilization of a larger political and economic entity.

2.4.3 The trade and investment effects of integration

The effects of integration described above are specific, at the level of the mechanisms described in Section 2.3. The impact of regionalism can be considered more broadly as well, in terms of its impact on the global system. The broader impact of regionalism is often described in terms of openness (Pelkmans, 1997; Van Tulder and Audet, forthcoming), despite a lack of clarity as to its meaning. Openness is looked at in different ways, e.g. in terms of openness to new membership or openness to trade (creation vs. diversion), which is effectively a question of ‘inward- or outward-looking’ regionalism (Pelkmans, 1997; Winters, 1993). Regionalism is considered open when the benefits of regionalism (or membership in the RIA itself) are open to third countries or competing companies from third countries (Haggard, 1997; Bergsten, 1997). At the national level, the World Bank uses an ‘openness index’ (OECD, 1996) which essentially measures changes in the import/export ratio. Such approaches are generally applied to RIAs as macro exercises. Regionalism is considered closed when intra-regional trade and investment substitute for extra-regional trade and investment. These substitution effects can be trade and investment creating or diverting, depending on whether lowest-cost producers fall inside or outside the RIA (Viner, 1950; Kindleberger, 1966).

Figure 2.2 shows how the imposition of a CET can change trade patterns between member countries as well as with non-members. The fictitious example deals with trade in bananas among three countries (A, B and C). In the pre-CET world, country A has a uniform tariff of 20 percent on banana imports. B and C are both banana exporters, with C producing units at $1.00 and B at $1.25, making C the lower cost producer. On the market in country A the bananas cost $1.20 and $1.50, respectively, after imposition of the 20 percent tariff. The three-dimensional arrows represent the volumes of trade between C and A and B and A, where C’s larger export share is a direct result of the price mechanism. When countries A and B decide to form a Customs Union and impose a common external tariff (set at 35 percent), demand responds to price changes and shifts in B’s favor with respect to C. With a 35 percent tariff, country C’s cost advantage disappears as consumers will always prefer

country B's $1.25 banana over those of country C. The three-dimensional arrows show how trade between A and B picks up while exports from C to A wither.

Figure 2.2: The static trade effects of a Common External Tariff (CET)

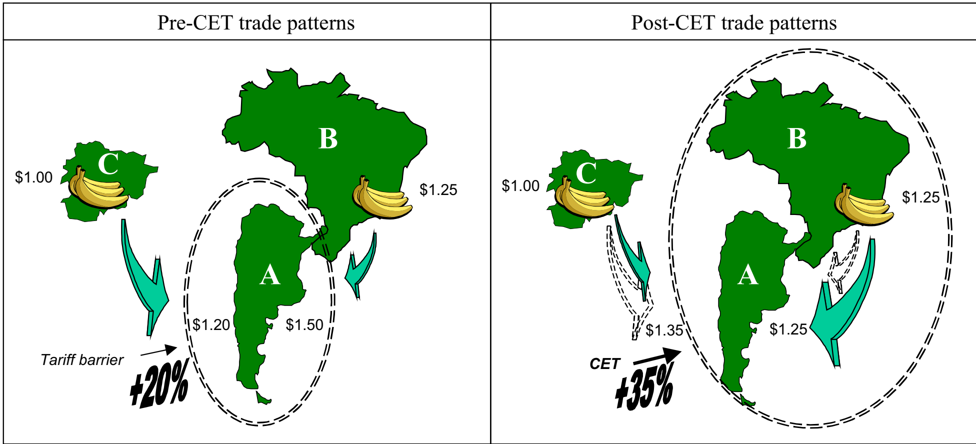
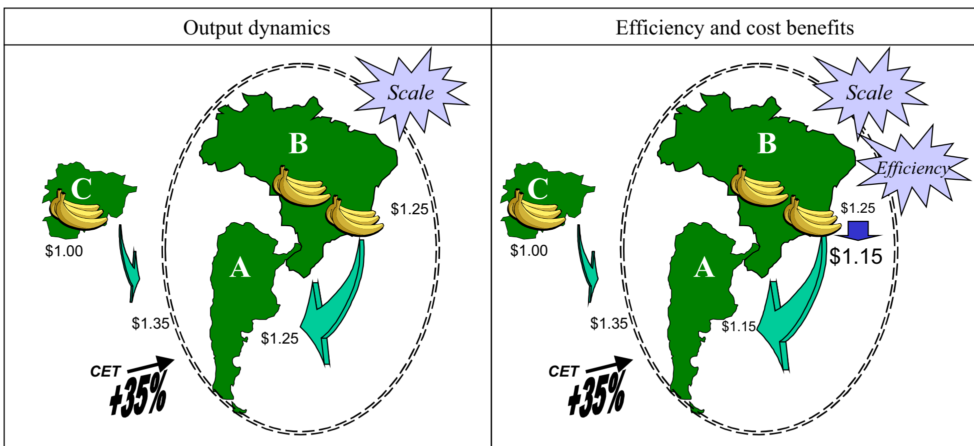


Figure 2.2 represents the 'one-off' or static trade effects of the CET, assuming that country B can instantaneously increase its exports to rebalance supply and demand. Production can be seamlessly adjusted and production factors are readily available for injection into the production process. As a stylized model it has inherent appeal, yet does not accurately reflect the reality of economic adjustment. In fact, this rebalancing is a dynamic process requiring a reallocation of resources in country B and specialization in banana production.
In Figure 2.3, the higher market price of country C's bananas on country A's market effectively creates a situation in which the supply of cheap bananas (now country B) is unable to meet demand (country A). Resources in country B must be reallocated to banana production to fill the void left by the exclusion of country C's bananas, and this specialization in the face of growing demand allows the banana industry in country B to profit from economies of scale (represented by the second bundle of bananas). Scale translates directly into lower production costs on the basis of efficiency (higher productivity), which are passed on to consumers as lower market prices. These welfare gains represent the benefits of comparative advantage based specialization under free trade. The gains, however, are not necessarily evenly distributed under free trade – reduction of tariffs and NTBs can reduce the tendency towards (inefficient) autarky, but it can also stimulate agglomeration and worsen the income and growth discrepancies, despite the often-made assumption that it will even out disparities. 'The dynamics of capital accumulation makes that the region with the higher capital stock ends up with the dominant industrial position' (Jovanovic, 2001: p. 26).
The effective exclusion of country C's exports from country A's market may generate an *investment creation* effect, if firms from country C respond to trade diversion by investing in production inside the region. If that investment comes at the expense of investment in other countries, it represents an *investment diversion* effect. Theoretically, then, this

treatment of trade and investment addresses both intra-regional and extra-regional effects, but in both cases relative to market access and market conditions *within* the region because they pertain to the search for sources of imports. There remains the question of the 'inside-out' effects of integration, or that of integration's effect on non-member countries as destination markets for goods and destination markets for investment. Blomström and Kokko (1997) argue conceptually that inside-out effects will depend on preexisting trade relations and the investment behavior of firms from within the region, yet note that there is a lack of attention for such effects in the literature. As McDonald and Dearden (1994) assert, this relates to the *ceteris paribus* assumption that nothing in the rest of the world changes and therefore is not relevant.

Figure 2.3: The dynamic effects of a larger market



Ultimately the degree of openness depends on barriers to entry in terms of e.g. consumer markets, labor markets, assets, resources, and technology. Bergsten (1997) defines true openness as the granting of MFN status to all members' trading partners. Unfortunately this has serious 'free-rider' implications (ibid.). Furthermore, his extreme suggestions for regional openness are in fact so open that it is dubious to what extent they represent regionalism at all. Bergsten's exemplary case of openness is that of APEC, the Asian-Pacific Economic Community, encompassing 21 countries with a sheer minimum of institutional foundations. Bergsten erases the boundaries of the regionalism vs. multilateralism debate, because his definition of open regionalism might just as well apply to the WTO, i.e. a region is only considered open when it is in fact not a region at all.

2.4.4 Empirical evidence of integration outcomes

The initial evidence of outcomes of integration can be observed in terms of all the (first wave) regions that in practice failed to generate real economic results, and as a result were not truly consolidated or institutionalized. Jovanovic attributes 'failed' integration schemes to one of several causes: overdependence on trade with countries outside the region; an

internal market too small to support scale and industrialization; high costs of transportation and poor communication; a central system of integration planning too far removed from market signals. The reasons for failure in past integration schemes suggest that economic and political factors are intertwined in determining outcomes, and the 'success' or 'failure' of integration.

Trade-theoretic approaches most often use Applied General Equilibrium (AGE) models to predict and analyze the impact of RIAs (Gatz, 1997; Bowen *et al*., 1998; Willenbockel, 1994). Whereas earlier empirical tests concluded that RIAs could be welfare-enhancing, (Lipsey, 1960), reexamination has suggested that the global and national welfare effects generated by free trade for some as opposed to free trade for all appeared considerably less certain (Bhagwati, 1993). Empirical studies with respect to the trade effects of integration are generally mixed and largely inconclusive (Gilpin, 2001; Bhagwati, 1993). Miller and Spencer (1977), considering UK accession to the European Community, predicted a loss in UK welfare using a general equilibrium model, and Viaene (1982) predicted EC membership in the Spanish case would result in a decline in GDP. Jacquemin and Sapir (1988) reported overall trade creation in a study on intra- versus extra-regional trade in Germany, the UK and France over the period 1973-1984 (cited in Bowen *et al*. 1998). Even with twenty years of hindsight the conclusions are ambiguous.

Extensive empirical analysis has been conducted on the impact of the 1987 Single European Act (SEA) on FDI flows into Europe from the US and Japan (Clegg and Scott-Green, 1999; Barrell and Pain, 1999; Belderbos, 1997; Morsink, 1997; Dunning, 1992; Yannopoulos, 1992; Lipsey, 1990) and to a lesser extent NAFTA (Blomström and Kokko 1997; Gestrin and Rugman, 1994). In this view, an RIA functions as a magnet for economic activity (firms) from outside the region. This is also a result of the 'locking in' function of an RIA (Atkinson, 1999; Yeung and Perdikis, 1999; Ethier, 1998). For intra-regional activity, Baldwin (1997) considers a combination of static and dynamic effects, which he distinguishes as 'allocation' and 'accumulative' effects, respectively. The former include terms of trade, volume of trade, trade rents, pure profit, scale and variety, while the latter are comprised of capital formation, foregone consumption and technical spillovers (Baldwin, 1997). Results have been largely inconclusive and focus on relatively outdated (pre-1992) data. The vastness of the literature on RIAs and FDI is quite possibly one of the reasons why empirical evidence remains inconclusive. Other studies have considered spread and agglomeration of activity. Jovanovic (2001) cites studies on the SEM program, concluding that the evidence is mixed and inconclusive. The only relatively undisputed conclusion is that the SEM led to an increase in inward FDI in Europe (Dunning, 1997a).

2.4.5 Regionalism: multilateral 'building blocks' or 'stumbling blocks'?

The debate on 'openness' and economic outcomes is usually considered in the context of regionalism as an alternative to 'multilateralism'. In the regionalism versus multilateralism debate, arguments focus more on the distribution of rents relative to extra-regional parties. Regional integration is analyzed in the context of the explicit assumption that RIAs are by definition 'second-best' welfare options compared to a (fictitious) state of global free trade (Bhagwati, 1993; Findlay in De Melo *et al*., 1993). At issue is whether regionalism is a 'stumbling block' or a 'building block' towards further multilateral trade liberalization on a global scale (Bhagwati, 1991). Political economists generally accept that deeper integration is bad for third parties. In classical economics approaches to (trade) policy, the

more and the freer the trade, the better. The welfare effects of free trade are good for everyone; 'the rising tide of free trade lifts all boats' (Leamer, 1995). In the neoliberal view, liberalization of world trade and investment is about benefits, not costs, yet critics emphasize the costs of globalization, such as growing income inequality both among and within nations, unemployment, environmental degradation and the negative impacts of unregulated financial flows on (particularly less developed) national economies (Gilpin, 2001). Similar arguments were made in the early functionalist approaches, which saw no limit to integrative tendencies, particularly the less governments intervened (cf. Mitrany, 1975).

More cautious approaches have demonstrated that limitations to multilateral free trade (i.e., trade blocs) can theoretically be constructed such that they are not harmful to non-members. Kemp and Wan (1976) broke new ground in this regard as the first generally accepted argumentation that RIAs were not necessarily inherently discriminatory to third parties. Some authors see macro-regionalism as 'one facet' of globalization, in which regionalism is a form of multilateralism, and not necessarily contradictory (Cox, 1994). The same issues play out in the debate on 'Triadization', i.e. whether trade and investment is increasingly centered on the world's dominant three trade 'blocs', the EU, NAFTA and Japan/ASEAN (Rugman, 2000) or spreading to other regions as well (Proff, 2002).

Regionalism and multilateralism, however, can be mutually reinforcing but still contradictory. The WTO (1995) admits that the *perceived* threat of regionalism played a key role in bringing the Uruguay Round of negotiations to a successful conclusion. Haggard adds that it is theoretically possible that regional arrangements 'are being negotiated by governments which already pursue relatively free trade policies on a multilateral basis, and in which free trade interests are strong. In such a setting, the dynamic with outsiders changes significantly. The source of discrimination is not so much the wedge between internal free trade and tariffs toward third parties, but the advantages that accrue to the community from other forms of policy coordination' (Haggard, 1997: 30).

However, Haggard (1997) also points out two reasons why the Kemp and Wan arguments may be flawed. First, because countries may be tempted to exploit the market power that is created by such a region, and second, as a consequence of the political bargains required to reach the regional agreement in the first place. In terms of the latter case, trade creation is a political liability, whereas trade diversion services producer groups within the region. Theory aside, regionalism in a historical perspective has almost always meant a loss of market access for external partners (Mattli, 1999b). Regionalism in the 1930s, for instance, is commonly associated with protection and conflict. Bergsten (1997) points out the examples of the British Commonwealth System of Preferences as well as the closed economic zone created in central Europe by Nazi Germany. It is not clear from his arguments, however, whether closed regionalism in this sense is considered a stabilizing factor (e.g. the British Commonwealth) or destabilizing factor (e.g. Nazi Germany). Bergsten also emphasizes the fact that in recent regionalist experiments, trade creation has generally exceeded trade diversion. Furthermore, RIAs can be a low threshold stepping stone for (especially developing) countries that wish to liberalize, and RIAs create an incentive for other countries to follow suit and 'ratchet up' the global process (Bergsten, 1997: 3).

Expectations of what other actors will do are crucial. This depends on whether they are already members of a regional agreement. According to Winters (1999), countries have

three possible responses to the regionalism of others: either to join an existing group, to create a new group, or to pursue multilateral liberalization (cf. also the preceding discussion on the 'ideal number of members' and 'bad regionalism'). The observation that integration has generally arisen from a backdrop of economic hardship and difficulties (Mattli, 1999a) reinforces the argument that self-interested behavior underlies the formation, and therefore the logic, of regionalism. As the international economy has become more closely integrated, regional groupings of states have increased their cooperation in order to strengthen their autonomy, improve their bargaining positions, and promote other political and economic objectives (Gilpin 2001, Balassa 1961). In this way regionalism can be seen as a form of global oligopolistic competition (market power), in which regions, at least partly, can be seen as a strategic response to regional steps by other blocs (Prakash and Hart, 1999).

Winters' (1999) response to the 'regionalism vs. multilateralism' question is simply 'we don't know yet' (p. 7). He bases his argument on three observations: 1) that models go both ways and are too abstract to be considered realistic; 2) we are faced with a shortage of real-life examples; and 3) no-one seems able to offer a functional definition of multilateralism. Bergsten emphasizes the fact that ultimately governments themselves, given the constraints of domestic and international interests, and the expected behavior of economic actors and other governments, have the ability to determine whether regionalism will result in greater multilateral liberalization or not: 'the inherent dynamics of the process seem to be sufficiently balanced that the policy decisions of the participants themselves are determinative' (Bergsten, 1997: 3).

2.5 Missing links

Mainstream approaches, besides being rooted in different fields of social science, demonstrate a wide range of theoretical assumptions and points of departure. Some theories focus on the causes of regional integration, and others on its effects. Yet none has generated conclusive evidence, and none has led to a convincing general theory of the phenomenon. This is even more glaring in light of the questions in regionalism today. Why and how do developing and developed countries integrate? Why is there such a wide range of institutional outcomes? Why is there a wider range of policy issues beyond those of trade? Why are extra-regional issues still ignored, though they seem more important than ever? Why are the strategic aspects of regionalism still 'masked' behind classical economic arguments? The inability to answer questions such as these has to do with three interrelated key 'missing links' in the literature: first, a lack of attention for firm-level strategies with respect to regionalism; second, an overemphasis on 'intrinsic' arguments for integration and a tendency to downplay 'extrinsic' motivations; and thirdly, a general failure to compare and contrast the rationale of government policymakers (intentions) with the actual restructuring behavior of firms.

2.5.1 Firm-level strategies with respect to regionalism

Traditional approaches to regional integration based on Viner (1950), Meade (1956) and Balassa (1961) overemphasize macro-level trade-theoretical elements (Dunning, 1997; Markusen, 1995; Findlay, 1993), while the true micro issues (i.e., the significance of regional integration for individual companies), even in *ex post* analyses, remain

understudied (Davies *et al.*, 1999; Phelps, 1997; Panić, 1991). These largely economics-oriented approaches introduce a simplistic understanding of economic activity without a geographic component, in which company behavior is derived from assumptions of 'markets' and the 'invisible hand'. Although more recent theories such as Strategic Trade Theory (Krugman, 1986) and economic variants of political economy (Panagariya and Findlay, 1996; Levy, 2000) make more effort to explicate both firm and government behavior, they remain highly stylized. Foreign Direct Investment (FDI)-centric 'dynamic' approaches (e.g. Blomström and Kokko, 1997; Cantwell, 1993; Yannopoulos, 1992) that build on Kindleberger (1966) highlight both macro and micro motives in regional integration, but assume by default that macro and micro actors are subject to identical problems and solutions.

In reality, the assumption that micro behavior is simply a disaggregate of macro trends (or the converse) reflects once again the bias of a one-dimensional approach. Vital issues of e.g. strategy and underlying market structure in traditional trade and FDI approaches remain a macro-level exercise based on abstract models far removed from the reality of individual companies (see Bowen *et al.,* 1998; Willenbockel, 1994). This is at least to some degree related to the debate on the substitutability between trade and investment, which in classical economic approaches and many policy models are still often assumed to be perfect substitutes. Some authors, on the other hand, suggest that trade and investment may be complementary instead of substitutable (Molle and Morsink, 1991; Blomström and Kokko, 1997) or in fact both (Blomström *et al*., 1998). As a result theory and empirical evidence about the net effects of RIAs on investment lead to no unambiguous conclusions. The lack of conviction is related to the lack of concreteness in establishing the relationship between trade and investment, which itself is a consequence of the abstract nature of working with such highly aggregated concepts to make firm-level inferences. Ultimately the relationship between trade and investment depends on the motives of both, which are best analyzed at the firm level (Goedegebuure and Van Tulder, forthcoming).

The persistent theoretical and empirical ambiguity can be seen as evidence that macro questions do not necessarily lead to micro answers. In the words of Braithwaite and Drahos (2000, p. 21), 'macro-macro theory tends to use abstract categories of explanation which appear to be more universal and seemingly allow theories to sweep across a larger range of phenomena'. The macro-level focus in mainstream theories of regional integration is symptomatic of the lack of explicit attention for both economic and political actors in the process and outcomes of integration. Regional integration is rarely placed in any kind of context and the 'hows and whys' are not addressed (Hettne and Söderbaum, 2000). Some approaches, like the New Economic Geography (NEG), emphasize firm-level responses to 'regionalizing' forces, but as in more traditional trade and FDI literature, companies are highly stylized, seen as rational, economic and without body. Moreover, it fails to address systematically the role of companies in the shaping of policy outcomes, i.e. the interaction between macro and micro actors in regionalizing processes. An understanding of regionalism requires the recognition of firms and governments as strategic actors in regionalism processes, with desired and expected outcomes, and explicit incorporation into frameworks and models.

2.5.2 Intrinsic and extrinsic motives for regionalism strategies

Given that governments and firms are strategic actors in processes of international restructuring, their interests and behavior are best considered from a strategic point of view. Political economy, strategic trade policy and public choice theories contribute much to our understanding of strategic interests, but tend to overemphasize trade, and sacrifice plausibility and real-world applicability for rigor. In most economics approaches, strategic considerations such as market power are often left out (Sachwald, 1993), in addition to economically 'sub-optimal' behavior like dumping and preemption (Gilpin, 2001), and location remains a neglected factor (Dunning, 1998). Thus the literature tends to overemphasize the 'bright side' of firm behavior (Eden and Lenway, 2001).

Political science approaches more specifically address actors and the context of actor behavior. Classic state-centric perspectives on regional integration like intergovernmentalism (Moravcsik, 1998) see states as actors and allow for the notion of suboptimal outcomes, yet oversimplify the role and interests of economic actors (the 'demand' for integration as opposed to the 'supply' of integration on the policy side; cf. Mattli, 1999b) and do not explore them empirically. Neoinstitutionalism (Keohane, 1984) views the origin and functioning of all types of institutions as the result of the welfare-maximizing behavior of rational individuals attempting to solve collective action problems, but despite its behavioral insights has not yet led to a specific theory of regional integration (Gilpin, 2001). (Neo)functionalism (Mitrany, 1975; Haas, 1958), on the other hand, sees states and governments as obstacles to what would otherwise be a bottom-up process for solving coordination problems, but emphasize transnational society as the major driving force behind integration while underplaying the significance, and potentially suboptimal behavior, of companies as actors.

Therefore, the logic of integration as explained by the mainstream theories reveals an overemphasis on 'intrinsic' drivers of firm and government behavior and neglects 'extrinsic' motivations. Intrinsic drivers refer to efficiency-oriented, rational, economic considerations determined by relating the state of affairs internal to the actor (e.g. production processes) to some often idealized 'Pareto optimum'. Extrinsic motivations, on the other hand, relate actor-internal issues to the environment or the behavior of other actors. The search for extrinsic motivations of internationalization is part of an International Political Economy tradition. Firm strategic elements involve e.g. the possibility of lobbying not only for a decrease in intra-regional barriers, but also for an increase in extra-regional barriers. Bargaining models of various types (Kobrin, 1984; Encarnation and Wells, 1986; Doz, 1986; Stopford and Strange, 1991) have addressed power-based motives for interaction, particularly between MNEs and developing country governments, but not yet in the context of regional integration. Extrinsic motives for company and policy strategy have been relatively ignored since the 1960s and 70s, when Hymer (1976) and others addressed the collusive, anti-competitive behavior of US multinationals. The International Business literature has focused largely on intrinsic motivations since the 1980s, emphasizing internalization of markets, economies of scale and scope, transaction costs and other internal coordination problems. In the same period, macro-economic and political science theories revealed a comparable logic, focusing on welfare gains from reduced trade barriers, efficiency effects and increased intra-regional competition.

Table 2.6, drawing on the origins of Regionalism as reviewed in Section 2.2, categorizes the motivations of governments for integration as intrinsic or extrinsic. Integration, for instance, can be motivated by the desire to link supply and demand at the regional level, lowering costs and freeing up resources for new growth and enhanced welfare. At the same time, integration may be motivated by a desire to enhance bargaining power in interactions with other states or regions. Additionally, Table 2.6 suggests that *companies* may favor regional integration on the grounds of intrinsic and extrinsic motivations as well, building on the 'missing link' identified above in section 2.5.1. Intrinsically, companies may see advantages in terms of reduced uncertainty and lower transaction costs. Extrinsically, regional integration can *de facto* raise barriers to entry for competitors from outside the region, or even enhance a firm's competitive position relative to others *within* the region. Ultimately, intrinsic goals do not themselves exist in a vacuum; rather, they are often pursued to serve extrinsically-driven ambitions. Similarly, extrinsically-oriented strategies may be pursued to *avoid* pursuing intrinsic strategies such as rationalization or downsizing.

Table 2.6: Examples of extrinsic and intrinsic motives behind regional integration

	Governments	*Companies*
Intrinsic intent • efficiency oriented	• neo-liberal policy orientation • reduce barriers to regional trade • increase intra-regional competition • couple supply and demand at regional level to create virtuous growth regimes	• more efficient resource allocation through regional division of labor and larger 'home market' • economies of scale and scope • mkt internalization; lower transaction costs • technical spill-overs • more resources available for innovation
Extrinsic intent • bargaining-power oriented	• improve bilateral bargaining position vis à vis other regions or hegemonic powers • improve bargaining position in multilateral forums • recapture lost ground of national autonomy • create institutional counterweight to cross-border activity of companies	• raise barriers to entry • create 'defensible' institutions and / or governance regimes • enhance competitive position (without downsizing) • springboard for extra-regional expansion to pressure stakeholders • regional 'location tournaments' to pressure stakeholders

2.5.3 The relationship between policy intent and realized company strategies

By and large, the literature either focuses on the origins of regional integration and neglects its effects, or expounds (largely theoretically) on the impact of integration while ignoring the origins. It is increasingly acknowledged that explanations provided by the dominant politically-oriented schools of thought, neofunctionalism and intergovernmentalism, are in themselves insufficient (Mattli, 1999; Cowles, 1995) and have generated only unconvincing attempts at synthesis (Branch and Øhrgaard, 1999; see e.g. Cameron, 1992 and Moravcsik, 1993). Political approaches, in their enthusiasm to understand the *process* of regionalism, are often 'far too vague on the question of what purpose a process serves if it is not to generate outcomes' (Winters, 1999: 9).

In most economics approaches, RIAs are treated as exogenous, or simply a result of a natural, deterministic tendency towards integration based on rational economic behavior. Regional integration is rarely placed in any kind of context and the 'hows and whys' are not addressed (Hettne and Söderbaum, 2000), specifically in terms of government roles

(Dunning, 1997b). Where regional integration is treated as a strategic issue, the motives and dynamics of its genesis are simplistic, and the role of economic actors is underdefined. In other cases it is generally associated with a positivist strategy motivated either by the desire to increase national and regional power, or to overcome market imperfections and enhance welfare in general. Explanations which emphasize domestic interests trying to shift rents in their own favor do not take into account costly exercises like the EU (Gilpin, 2001).

Finally, attempts at integrating insights from political science approaches with insights from economics approaches are few and far between (see e.g. Baldwin, 1996). The debate on policy-induced integration versus integration stemming from economic forces (Mansfield and Milner, 1999) may also be of limited use in understanding the impact of true integration, because true integration implies policy cooperation as well as economic restructuring. An understanding of the phenomenon requires an appreciation for the intentions of the policymakers as well as the realized changes in the organization of economic activity by firms. This requires some perspectives on the way policy is intended to impact firms, what the assumptions exist among governments regarding the drivers of firm behavior and responses to policy stimuli, as well as attention for the nature of government – firm interaction. International restructuring, however, is not limited only to those issues that governments consider to be on the agenda for discussion with the governments of other states (Strange, 1997a). Firms have strategic considerations of their own that governments may or may not take into account. As a result, political and economic actors can have different, and sometimes conflicting, strategic motivations. Hence governments, in their attempt to manage economic behavior through the building of institutions, risk anticipating different strategic behavior than in reality takes place, such that realized restructuring outcomes may differ from those expected by policymakers.

3. UNDERSTANDING THE DYNAMICS OF REGIONALISM

This chapter redresses the missing links in understanding the particular dynamics of regionalism identified in Chapter 2. The first two sections propose ingredients for a more holistic approach to the phenomenon of regionalism, resting on the tension that exists between the strategies of governments and 'core companies', the key economic actors involved in international restructuring. Section 3.3 explores the logic of government regulation in the spatial organization of economic activity, and section 3.4 discusses some of the issues that determine government policy preferences with regard to international institution-building in general and regionalism in particular. Section 3.5 explores different levels of policy interests and develops a new typology of RIA policy strategies that governs both intentions and realized outcomes. The chapter concludes in 3.6 by paving the way for integrating the policy-level typology with one at the core company level (Chapter 4).

3.1 Towards an integrative, macro-micro approach

Understanding the origins and impact of regional integration is quite complex. Regional integration is both a matter of policy shifts and changing patterns of economic activity, and must be analyzed as such. Carr (1951) observed that 'the science of economics presupposes a given political order, and cannot be profitably studied in isolation from politics' (quoted in Gilpin 1975: 37). Waltz (1979) argues that economic theories tell us something about politics and political theories tell us something about economics. The study of economic and political forces interacting to shape the economic and political order requires the application of institutional perspectives. 'An analysis of regional integration that neglects to incorporate institutional elements risks being empty. [One] must consider the reciprocal relationship between economic and politico-institutional factors' (Mattli, 1999: 7). If regional integration is seen as an institution-building exercise with both a process and outcome side, a framework needs to be developed that addresses the actors involved in the process, their strategic interests, the nature of their interaction, and allows for evaluation of the outcomes.

3.1.1 Actors and strategy in supranational institution-building

An institution is 'an ongoing organized human activity that has some fundamental societal purpose' (Wartick and Wood, 1998: 22) and provides incentive structures that determine social, political and economic behavior (Gilpin, 2001; North, 1991). Many mainstream approaches to regional integration assume that the market is the primary force organizing economic behavior (Gilpin, 2001), and assume away the relevance of institutional and political forces. Those which do consider institutions assume they are primarily created either to support the market by increasing its efficiency, or for maximizing the welfare of individual actors (CPB, 1997; North, 1991). Others see institutions as a coordination issue in the absence of a power center (e.g., a hegemonic state), or a 'regulatory regime' for solving collective action problems (cf. Keohane, 1984). Yet it is possible that institutions are formed for rational, irrational or even capricious motives, or as an unforeseeable outcome of historical accident and path dependency (Arthur, 1989). Hence institutions may

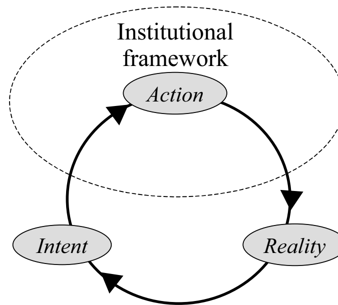
not be a direct representation of the interests of the actors that created them (Gilpin, 2001; Schotter, 1981).
Institutions may be spontaneous (international common law), but they are most often the result of (intentional or unintentional) interaction between a range of actors. Often game-theoretic approaches are used to describe the emergence of institutions (Schotter, 1981). Institutions can thus also be seen as a means of organizing relationships between actors (Cox, 1989). This organizing quality can be found in the understanding that institutions are 'sets of implicit or explicit principles, norms, rules and decision-making procedures *around which actors' expectations converge in a given area of international relations*' (Krasner, 1982 cited in Gilpin, 2001: 83; emphasis added). The term 'actor' in this study is used in the sociological sense to describe a group of individuals sharing the same interest (Cyert and March, 1963). Regional integration, as a process of international restructuring, is a matter of actor interaction in (re)defining 'the rules of the game'.
If an actor is considered 'a group of individuals with the same interests', strategy can be seen as a 'deliberate act of a collection of people joined together to pursue some mission in common' (Mintzberg and Waters, 1998). Therefore, strategy can equated with action. If institution-building is about actors defining the rules of the (common) game, it can be said that actors join together to pursue a 'mission in common', i.e., the establishment of a new institutional framework, and through their actions consolidate that framework. Organizing actor relationships in such a way that expectations should converge suggests that norms, values and behavior should converge as well, otherwise expectations would increasingly diverge from reality. Following this line of thinking, institutions are about actors doing the same things according to the same rules. In this sense institution-building is intended to reduce uncertainty.

3.1.2 A holistic perspective on strategy

The Strategic Management literature describes processes of 'strategy formation' as identifying a strategic problem, forming a diagnosis, conceiving a solution ('strategy formulation') and realizing that strategy (De Wit and Meyer, 1998). However, many approaches consider strategy as a linear process (Mintzberg and Waters, 1985). Linear approaches to strategy tend to overlook the fact that 'realized strategy' forms the basis for the next step. This is only the 'planned' part of strategy, which does not yet consider 'organic' (emergent) strategy. The degree to which strategy is seen as planned versus organic is based on assumptions of cognition, rational thought and bounded rationality, which is an issue of logic versus creativity, and of how 'controllable' the environment is. De Bono (1970) calls this vertical versus lateral thinking, or thinking 'inside or outside the box'. In game theory, strategy is a decisional rule that determines the decisions and actions an actor will take.
The strategy formation process described in the literature generally fails to consider the contextual aspects that determine how a problem is identified as such. 'Conceiving' is a step where strategic options are defined, which is not only based on a perception of an actor's strategic position, it must also involve assumptions of the behavior of other actors. Under institutionalist assumptions, the tendency exists to expect archetypal behavior on the part of actors. For instance, economic actors under a Customs Union, as an example of an institutional framework, may be expected to trade more with partners in fellow CU member states. Viewing institution-building as strategic convergence, however, may have

merits at some level, but risks placing strategy in a vacuum and generating ideal-type assumptions of a singular behavior.
Attention must be paid to the 'mission' and 'interests' of individual actors. Mission and interests are issues of *strategic intent*, or the 'goals and desires' (Braithwaite and Drahos, 2000) underlying specific actions. The goals and desires, which form a range of strategic options, do not exist in a vacuum nor are they defined entirely by the institutional context. Strategic intent is shaped *inter alia* by the *strategic reality* in which an actor operates. Strategic reality is a matter of perception, and how an actor identifies its own situation and the strategic problems it faces. In this way reality is 'framed' in such a way that it provides 'guideposts for action' (Rein and Schön, 1991: 263). An actor's strategic reality is in turn formed, *inter alia*, by the actions the actor has taken in the past. Thus strategy is a cycle of feedback loops in which reality shapes intent, which influences action, which in turn again influences reality (see Figure 3.1). In strategy, in other words, history matters.

Figure 3.1: Strategy feedback loops



This remains a very generic approach to strategy which is not intended to suggest that actors act in isolation. Exogenous factors still influence actors' actions, reality and intent. The central argument here is that the environment and the institutional setting do not determine a single universal behavior, because actor behavior is shaped by the circumstances particular to individual actors. In the Customs Union example, a wider range of strategic options beyond that of simply increasing exports is available to individual economic actors (firms), depending on their strategic intent and the strategic reality in which that intent is rooted. This palette of strategic options, or strategic repertoire, may be shaped by a given institution (e.g. the Customs Union), but is determined by other factors as well.

3.1.3 Core companies as key actors in institution-building

There is a great deal of attention for the policymaking side of regional integration, but this is rarely linked explicitly to firms. On the one hand firms do not receive enough attention for their proactive role in policymaking, on the other hand, firm-level responses to policymaking underconsidered (Davies *et al*., 1999; Phelps, 1997; Panić, 1991). The role of powerful economic actors and governments in e.g. the SEM is well documented (Balanyá *et al*., 2000; Criekmans, 1998; Cowles, 1995), with special attention being paid

to the role of organized forms of political activity such as the European Round Table of Industrialists (ERT) in the integration process. Several other business organizations exist in which core companies figure prominently, such as Transatlantic connection, the Group of Thirty, the World Economic Forum, the Business Roundtable. Overemphasis on such organizations as actors in their own right, however, has led to a tendency to focus on the umbrella institution instead of the individual members.

It is conceptually stronger in this sense to think of key economic actors as 'core companies' (Van Tulder *et al*., 2001), of which organizations like the ERT are merely the best-organized vocalization. Many macro-economic developments, for instance, are in fact the expression of the strategic behavior of a limited number of core companies. For instance the case of world FDI stocks, where 50 firms account for more than 60 percent of total US outward FDI stock; the case of trade, where between 30-60 percent is thought to be company internal trade and thus open to transfer pricing; and in Research and Development and patenting strategies, where more than 50 percent of R&D expenditures in many nations are accounted for by only 5 companies. In many respects international restructuring processes are a 'small numbers' game (ibid:xx).

Thinking of large and multinational firms in terms of core companies is becoming increasingly popular in the International Business literature. John Dunning, for example, in his seminal overview work on Multinational Enterprises and the Global Economy, confirms the importance of linkages and spill-over effects and multinationals considered in their network configuration (Dunning, 1993: 445ff). Other definitions of 'leading firms' in combination with network configurations exist such as 'leader firms' (Porter, 1998) or 'flagship firms' (Rugman and D'Cruz, 2000) in which multinational firms are characterized by global competitiveness and international benchmarks. A comparable discussion is triggered by the introduction of the idea of meta-national companies. Core companies are large firms that operate as spiders in webs of value chains and innovation, lead processes of internationalization and which – partly due to their core position – also have explicit political vision and direct access to political decisionmakers (Cowles, 1995). 'Core companies' are operationalized in greater detail in Box 1 below.

It generally acknowledged that in particular large firms are powerful actors in political and economic processes and outcomes (Hancher and Moran, 1989). Core companies are key actors in regional integration, both in terms of the processes that underlie integration origins as well as the restructuring that signals the outcome of integration. This means core company strategies have economic and political, or market and non-market, dimensions (Baron, 2000). Core companies can employ proactive, reactive and interactive response choices to changing business-government relations (James Post [1976] cited in Wartick and Wood, 1998). Such choices can involve e.g. front-loading incentives for governments or threatening sanctions such as withdrawal (see also Doz, 1986). A proactive approach, for instance, increases the likelihood of influencing outcomes, but being reactive minimizes costs incurred from incorrectly anticipating change. It is also possible to have in some cases even inactive strategies, particularly if the core company's systemic power is significant enough. This means the firm's influence is so great that it need not take any action, or even threaten to do so, for the simple possibility that it can take such action is sufficient to sway governments and determine policy outcomes. On the other hand, core companies can use their leverage to play governments against each other (Doz, 1986). Additionally, there are push and pull elements to core company strategies: Molle and Morsink (1991) refer in this respect to strategies of stimulus and resistance to signal

support for or opposition to regulation initiatives. These can also be seen as voice and exit strategies (Hirschman, 1970).

Box 1: Key characteristics of core companies

- The first characteristic of a core company is its **sheer size**. A core company is amongst the firms with the largest sales volumes in its branch. In practice this condition implies that the sales volume of core companies measured on a global scale is more than $5 billion. For more nationally oriented core companies sales volumes of more than $1 billion can be expected
- A core company has **direct access** to domestic and foreign end markets and/or customers, either through subsidiary sales and service offices, or through third parties importing/distributing the core firm's product and offering service. A core firm will at all times be able to **license** and **control** the use of its own **trade mark** (except for criminal abuse);
- The management of a core company has an **explicit vision** of (1) the organization and management of the value chain, including the internal labor process; and (2) the **role of external actors** (such as banks and governments) in facilitating the creation of added value and the (re)structuring of the network;
- The vision of the management of a core company on the organization of its **external network** serves as an orientation point which it strives to accomplish. The logic of industrial restructuring within and between **networks** should be studied as an interplay between this vision and the core firm's ability to determine the rules of the game within the network;
- A core company has by nature a **high degree of relative independence** from other actors in the supply chain(s) it operates in. A core firm is generally one of the principal actors and more often the director of the play covering the interactions in the network. In some networks, a core firm may give up its role as the sole director, yet will always remain a leading actor, and, if given the opportunity, it will try to regain control;
- A core company owes its relative independence (1) to its control over a series of **core technologies** and other strategic competencies, particular to an industry or industrial activity; and/or (2) to its **financial muscle**;
- A core company will often be a **user-producer**, meaning that it not only produces new products or product technologies, but it is also among the leading users of these technologies.

Source: Van Tulder, Van den Berghe and Muller, 2001

The market-strategic dimension to being (or becoming) a core company requires both vertical and horizontal positioning decisions. Vertical positioning describes the part of the value chain a core company controls directly through in-house production or distribution. This refers to the degree of vertical integration (DVI) of a firm, the amount of outsourcing or the share of the total value-added which a given core company supplies. All three aspects refer to the same strategic choice.

Horizontal positioning refers to the number of branches a core company operates in, and thus the degree of diversification over a small or a large number of branches or sectors. Within sectors, the aim could be more or less differentiation in particular product ranges. While vertical integration, diversification and differentiation basically represent the strategic dimensions already identified by Michael Porter in 1985, horizontal positioning defines the share of economic activity which flows through a core company, regardless of the value added. Large retailers, for instance, may add relatively little value, but since they manage links between supply and demand on an extremely broad scale, their power can be quite extensive. Core companies in this way can exert distinct influence over chains and sectors by virtue of their positioning. This influence works two ways, however: it should be recognized that a firm's strategic behavior 'not only depends on the expectations it has about markets' efficiency or rivals' behavior, but may also directly aim to influence rivals' expectations about its future behavior' (Mucchielli, 1991: 50). The market oriented

'strategic realities' created through their behavior allow firms to influence the strategic realities of policymakers, thereby influencing the direction of institutional development.
Non-market techniques like lobbying lead to lower transaction costs (psychic distance, cost of information) but also offers those firms with an active lobby a competitive advantage in creating a policy environment best suited to their needs. Lobby activity takes place through trade associations, head of industry organizations, peak associations or professional lobby agencies. In the US, for example, the right to lobby is part of the 1st Amendment, and interest groups spent nearly $700 million in 1999 lobbying Washington alone. The very act of lobbying may influence strategy as well, as it has been proven that having a local office helps when trying to lobby a government (Baron, 2000). Other factors that improve the chances of impacting decisions are e.g. through direct access to parliamentarians or members of Congress, or, indirectly, through reputation, credibility, and market power. Non-market techniques tend to involve lower costs than market techniques because of the degree of uncertainty and risk-mitigation involved. Lobbying essentially reduces uncertainty against a fixed cost, while market techniques create a built-in risk and may result in less than optimal production strategies. Thus market strategies influence outcomes and non-market strategies influence policy itself: these are in fact 'push' and 'pull' elements of strategy.

3.1.4 Strategy in policy space versus competitive space

The traditional literature on regional integration shows how levels of actors can be confused, because it demonstrates how theory infers micro-level behavior from macro-level strategies. At the macro-level, the strategic intent behind a Customs Union (CU) may be to increase trade with CU partners, given e.g. a strategic reality of declining terms of trade. Despite the assumption referred to above that 'actors' expectations converge' under a given institutional setting, it is simplistic to assume that actors share motives for the formation of any given institutional framework, or that they will complement each other's strategies for capitalizing on that framework. As Streeck and Schmitter (1996) demonstrated in the case of the SEM, although European business and government elites joined forces, each did so for different reasons. Central to institution-building is the tension between strategies of the key actors involved.
The tension between actors involved in restructuring stems largely from the difference in 'spaces' within which actors operate. Space is used here in the more abstract sense of Perroux's (1950) 'field of forces', or Cohen's 'authoritative domains' (Cohen, 1997) than purely in the physical sense. Governments, for instance, are primarily concerned with governance structures within a geographically defined policy space (similar to 'regulatory domains' of Braithwaite and Drahos, 2000; and the 'political space' of Dunning, 1997). Core companies, on the other hand, are concerned with the activities which take place within their competitive space, in particular that segment of their competitive space which they attempt to control (Ruigrok and Van Tulder, 1995). Competitive space is best understood as the arena in which firms compete (similar to the 'contestable market' (Baumol, 1982)), with specific rules of engagement that reflect the characteristics of competition between firms. Competitive space can exist at the industry level or e.g. among a relatively small oligopoly within an industry, depending on the make-up of the industry and how (market) power is concentrated. Policy space can be characterized as a 'macro' space due to its national orientation and corresponding high levels of aggregation in

analysis, while competitive space is best seen at the firm- (or industry) level and can be qualified as a 'micro' space (cf. Figure 3.2). Policy space and competitive space may overlap and interweave through geographic space but are not necessarily spatially organized in complementary ways (cf. Dunning, 1997). Given the differences in their macro and micro operational spaces, companies and governments do not face the same strategic realities, nor do they have the same strategic intent (Eden, 1993; Rugman and Verbeke, 1991). Realities are not always self-evident; they are to some extent theorized. Additionally, they are constituted by knowledge structures that give identity to institutions and forces (Gill, 1994 in Underhill, 1994).

Figure 3.2: Strategy in policy space versus competitive space

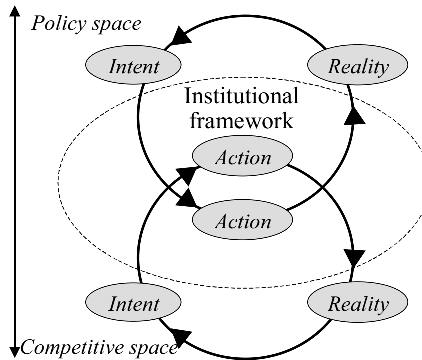


Figure 3.2 shows that macro reality and intent exist in a different sphere than that of micro actors, though they both act within a shared institutional setting. In addition, the figure suggests that the strategies of economic and political actors are intertwined in the formation and consolidation of new institutions, reflecting the notion that geographic and competitive space interweave and overlap. Governments shape economic behavior, not only through policy, but also through strategic geo-political maneuvers (Van der Pijl, 1992). At the same time, free market systems mean that firms take decisions beyond the realm of government control (Criekmans, 1998). Additionally, companies themselves affect the development of the very institutions which govern their activities (Zylberstaijn and Jank, 1998) through both market and non-market strategies (Baron, 2000). Phelps (1997) refers to the influence of companies, and particularly MNEs, on regulatory institutions as 'institutional or regulatory capture'. Building international institutions like RIAs involves the push and pull forces of macro and micro actors through geographic space and competitive space. Regional integration is a matter of the internationalization strategies of governments and core companies.

3.2 The macro/micro dynamics of Regionalism

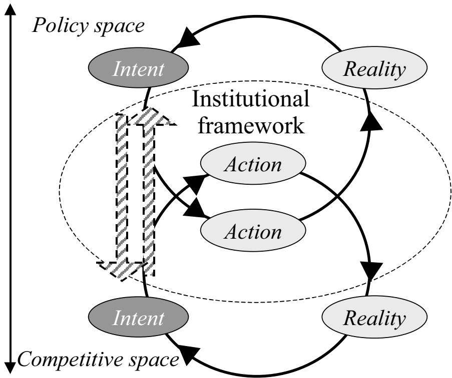
A change in institutional setting not only alters the way in which activity (in particular economic and political) is organized, but also the way in which actors interact in pursuing their interests. In the formation of new institutions, the confrontation between stakeholder interests is played out in bargaining environments (Ruigrok and Van Tulder, 1995),

generally characterized at the national level (Whitley, 1992; Porter, 1990) by the degree of cohesion in stakeholder interests (the 'stakeholder nexus', Van Iterson and Olie, 1992). In such restructuring processes, governments and firms are the most important actors (Vernon, 1994).

3.2.1 Mutual (mis)perceptions of strategy

At the same time, macro and micro actors possess perceptions and assumptions of one another's strategic intent. Micro actors anticipate certain policy measures, and macro actors anticipate certain shifts in economic and productive behavior. This links the action of one actor to the intent of another actor by drawing on the notion of reciprocity, meaning that a given actor has an interest in (and expectation of) other actors performing a given action (Braithwaite and Drahos, 2000). This interest (and expectation) is the basis for interaction (bargaining), as well as the strategic behavior which results from that interaction, and thus has consequences for the outcomes of the institution-building process (Figure 3.3). Misconceptions between the two levels of actors can lead to unanticipated behavior and thus to unexpected outcomes. Therefore, despite a common institutional setting, problems of e.g. bounded rationality and opportunism (CPB, 1997) are not necessarily 'solved' by a new institutional framework given the macro-micro dichotomy in institution-building. The notion that everything can be explained away by fully rational economic thinking fails to recognize that intent can be fully rational, but that actors, through the limitations of their own strategic reality, may not fully appreciate the reality and intent of other actors, which can lead to unexpected outcomes.

Figure 3.3: Perceptions of intent and assumptions of action



As Mintzberg and Waters (1998) point out, 'planned strategy' assumes also that the environment is controllable (or at the very least predictable). The ability to control is an issue of *power*. In assuming implicit controllability or predictability, micro and macro actors may project their own intent and reality onto each other, such that the level of analysis problem is expressed in terms of insufficient understanding of each other's strategies (Strange, 1994). Policymakers may see themselves as facilitating or regulating economic actors, depending on assumptions of the motives behind economic actor

behavior. They may see companies as e.g. extensions of policy, or 'politics by other means' (Vernon, 1971); on the other hand they may see them as threats to state power (Eden, 1993). Policymaking bodies will likely have an implicit view of companies, for instance as producers converting inputs to outputs to satisfy society's material needs and wants within a context created by government activities (i.e., policymaking). This implies that policymakers have a vision of firm-level reality and intent, and of their own role in managing that reality and intent.

Companies, on the other hand, may see their purpose in e.g. 'identifying and exploiting the resources and capabilities of the firm in the marketplace for the purpose of gaining competitive advantage and superior financial performance' (Tallman and Yip, 2001: 1), and perceive policymakers as managers of macroeconomic stability, inputs and infrastructure efficiency, the rules of the game and the negative consequences of monopoly power (Porter, 1998). Yet such assumptions place behavior in a contextual vacuum and ignore any intrinsic interests policymakers themselves have. Ultimately these perceptions underlie the strategic behavior of actors at both levels, as well as the way in which they interact with each other, and will be determinant for the outcomes of a given RIA regime.

The strategic mismatch present in this analysis of institutions draws conceptually on game-theoretic approaches to (explicitly determined) institutions. In this sense a game is a set of rules for a particular situation which delimits the actions available to the players. Each player has a set of actions he can choose from (the strategic repertoire). Payoff is determined not only by own action but also by the action of other actors. Schotter (1981) describes four kinds of problems that can lead to the emergence of social institutions: problems of coordination, prisoner's dilemma, problems of inequality preservation and problems of the cooperative-game type. This adds a new dimension to game theoretic approaches like the prisoner's dilemma, where uncertainty can lead to less than optimal behavior.

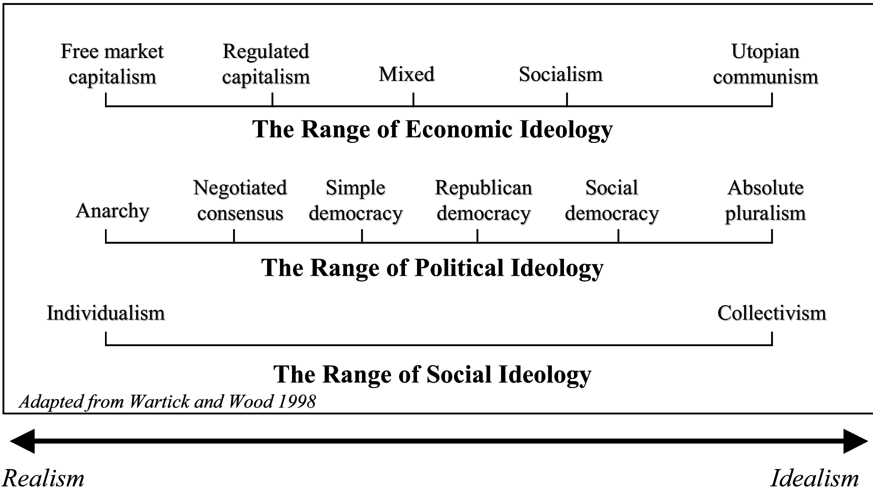
3.2.2 Underlying assumptions of behavior

Ultimately, strategy must be understood in the context of assumed motivations behind human activity, both at the macro and the micro level. 'Historical experience indicates that the purpose of economic activities is ultimately determined not only by markets and the prescriptions of technical economics, but also (either explicitly or implicitly) by the norms, values and interests of the social and political systems in which economic activities are embedded' (Gilpin 2001: 12). It is therefore essential to explicate the behavioral assumptions underlying actor strategies in order to place that behavior in the proper context.

Interests and behavior of the one can be related to the interests and behavior of the other as e.g. harmonious, adversarial, altruistic, self-interested or 'enlightened' self-interested (Baldwin, 1985). They can also be seen at varying levels, such as societal, economic and political. A useful framework for structuring interests, and institutions for that matter, involves positioning of societal values along the individualist–collectivist axis, economic values along the free-market–utopian axis and political values along the anarchist–totalitarian axis (Figure 3.4). In fact all three are dimensions of the idealism–realism axis in the sense of the classic Lockean-Hobbesian polarity (Van der Pijl, 1992). Classifying assumptions of behavior is not only a question of theoretical perspective; it also has implications for how macro- and micro-actors perceive each other and their respective

interests and strategic behavior. Governments may for instance implicitly ascribe certain behavioral drivers to the companies they target with policy measures (thereby generating assumptions of strategic intent) which do not correspond with the actual behavior of those companies. Such misperceptions of company strategy can also be a source of tension between macro and micro strategies, and ultimately lead to potentially unexpected outcomes.

Figure 3.4: Ideological continua



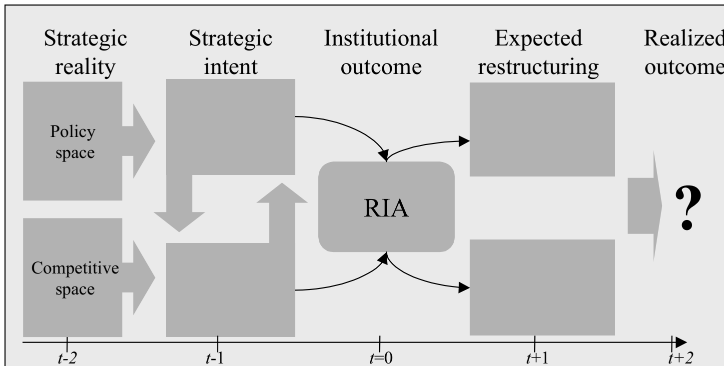
3.2.3 Institutional outcomes and restructuring outcomes

International restructuring as an issue of power makes it particularly attractive to think in terms of outcomes (Strange, 1997a). The outcome of Regional integration is an interplay of policy outcomes in geographic space and restructuring outcomes in competitive space. In other words the policy-level manifestation of the institutional framework (the RIA) is only an intermediary outcome which cannot be seen independent of the economic manifestation of that framework (restructuring of economic activity). It is not only the agreement of e.g. a Common Market that creates a regional institution, it also necessitates that actors behave accordingly (cf. Scott, 1995). The existence of an institutional outcome together with a restructuring outcome in fact determines whether the institution is successful (Mattli, 1999a). This links the process and outcome dimensions of regional integration. The relationship between process, outcome and power is supported by Strange (1997a), who essentially argues that power can be exercised in both the restructuring process itself ('structural' power, which determines the way the game is played) as well as in shaping the outcomes ('relational' power, by which one actor gets another to do what he or she wants). Process and outcome can also be linked by 'unrolling' the strategy feedback loops illustrated above into linear functions. Unrolling the loop creates more dynamism, because unlike the loop, the line emphasizes that strategic reality at the end of each loop is different than the strategic reality that preceded the loop. In other words, actions (i.e., strategic

outcomes) feed back into a slightly altered strategic reality, because through those actions the institutional context has changed. In this way strategic reality is ever-changing, and institution-building outcomes are given both a policy dimension and a dimension of economic restructuring.

This dynamic is illustrated in Figure 3.5. Essentially the figure represents the strategy feedback loops illustrated above, but then 'rolled out' into a linear trajectory. In this case strategic realities of governments and core companies, designated 'policy space' and 'competitive space' respectively, largely determine the strategic intent underlying behavior. Strategic intent defines the stakes of the game and thus the bargaining behavior (symbolized by the vertical arrows between 'strategic intents' in Figure 3.5). In their bargaining interaction (characterized by incomplete information), governments and core companies are to a large extent forced to make assumptions of one another's behavior. On the basis they reach an agreement as to the institutional outcome, which is in this case the formal Regional Integration Agreement. That outcome, and the stakes, are predicated upon assumptions of *resultant* behavior, which is in fact the restructuring outcome expected to complement the institutional outcome. However, the nature of realized restructuring remains to be seen, as action is subject to strategic behavior, incomplete information and assumptions regarding the strategic reality and intent of other actors.

Figure 3.5: Institutional and restructuring outcomes



In fact, the interplay between institutional outcomes and restructuring outcomes suggests a game of positioning, with characteristics of oligopolistic competition. Macro and micro actors jockey for position and, as companies in the traditional oligopolistic sense, 'react to one another in a direct and personal fashion' (Knickerbocker, 1973: 4). This recognizes, for instance, that some actors have more bargaining power than others, a function of e.g. size, geographic location, the promise of future market size and access, the degree of interlinkages with other actors, or the ability to dominate markets or value chains. Countries must therefore be seen as more than dots in space. For firms, there is a strategic component which is ignored by most economic arguments. If anticompetitive behavior such as dumping and preemptive investment occurs under regional integration despite expectations to the contrary, this may simply be a result of positioning strategies (Waverman, 1991). Positioning in turn implies that the field of actors is manageable and

not infinitely large; ultimately institution-building is a small-numbers game. The small-numbers game means there is more opportunity for direct bargaining interaction between actors. This can lead to more symbiosis at both macro and micro levels, but not necessarily *across* levels.

Strategic positioning in turn implies that outcomes can be sub-optimal in the classical economic sense. Conversely, it can be argued that an economically 'optimal' welfare construct is not necessarily optimal in the interest of individual actors. It can easily be assumed that in certain situations, certain macro and micro actors might see the classical 'second-best' strategy (RIAs) as leading to the most desirable outcome in terms of their own strategic interests. The theoretical welfare gains to the world of global free trade over RIAs may be largely established, but in practice the distribution of those welfare gains remains an issue (Gilpin, 2001). Moreover, regional outcomes may be subject to 'bandwagon effects' (Van Tulder, 2001) or 'path dependency' (Arthur, 1989) that may by themselves lead to suboptimal regions, or configurations of regions.

3.2.4 Regionalism as a policy-led, two-level game

In regional integration, key actors determine their behavior largely in response to and in anticipation of other actors' behavior. This is reminiscent of iterative mixed-motive games ('manipulative' bargaining games, as opposed to non-cooperative games, cf. Gawande and Hansen, 1999) that emphasize the 'presence of both strategic interaction and imperfect information' (Young, 1975; cited in Keohane, 1984). In such games strategic choices are not made in isolation but emerge based on expectations of other actors. Neorealism (Krasner, 1982) and neoinstitutionalism (Keohane, 1984) deal with these strategic choices in international relations. However, the neorealist emphasis on conflict and anarchy in international relations makes cooperation seem unlikely and does not explain the recent resurgence of Regionalism. Neoinstitutionalism is more optimistic in that institutions can become 'intervening variables' that create incentives for cooperation between states, but both theories tend to ignore the significance of the domestic arena in shaping international preferences.

Putnam's theory of two-level games form an attempt to link the domestic and international issues (Putnam, 1988; Cowles, 1995; Putnam, 1993) and has recently been used to analyze the dynamics of regional integration (Cameron and Tomlin, 2000). The two-level approach focuses on legislators and ratification procedures in international negotiations (Meunier, 2000). This is a weakly developed part of two-level game theory (Cameron and Tomlin, 2000). It also only deals with domestic politics, whereas we are dealing with the articulation of economic interests by core companies. The approach introduced here, therefore, introduces a different level than the level Putnam and successors are referring to. The game becomes a two-tier game similar to the two-level games of Putnam, but distinct in the sense that the focus in this case is between political and economic actors as opposed to Putnam's state-centric balancing act between international and domestic interests in negotiating supranational institution-building. Additionally, the current study does not attempt a formalized modeling of the bargaining dynamic. Two-level games, which Cameron and Tomlin (2000) describe as 'more metaphor than theory' (p. 25) and many of those who build on Putnam tend to oversimplify, are better suited to a conceptual approach.

Taking such an approach requires attention for theories of international relations as well as theories of economic governance and regulation. The focus here is primarily on the strategies and interests of political actors and economic actors (vertical) and less on intergovernmental interaction (horizontal), because although the latter is clearly relevant, ‘cross-national information asymmetries [in negotiating supranational institutions] are less prevalent than … mis-estimations within domestic polities’ (Evans, 1993; cited in Cameron and Tomlin, 2000: 22). Furthermore, the world of core companies must be explored to understand their strategic concerns as well as the means through which they can affect international outcomes (institution-building). Core companies can exercise real and powerful influence on government policy preferences, not only through political contributions and lobbying, but also through market mechanisms and (re)location strategies.

Addressing regional integration using a two-level game-theoretic perspective makes it more relevant to look at strategies in terms of extrinsic strategic intent than solely in terms of more traditional, purely economics-driven concepts. Ultimately, intrinsic goals do not themselves exist in a vacuum; rather, they are often pursued to serve extrinsically-driven ambitions. Similarly, extrinsically-oriented strategies may be pursued to *avoid* pursuing intrinsic strategies such as rationalization or downsizing. Extrinsic strategies can be collectively explored as ‘bargaining power’, defined in general terms as the ability of a negotiating actor to obtain the most from a partner while conceding the least, *ceteris paribus* (Meunier, 2000). For governments this implies the ability to dictate terms in other policy spaces and for core companies the ability to dictate competitive space, or the terms of competition (‘rules of the game’). Bargaining power is a useful perspective because 1) it follows logically from the strategic interaction, power and game theory precepts already introduced; 2) it has a spatial component in that size, reach and locational presence are important factors, which can easily be related to the restructuring aspects of integration; and 3) bargaining power, having also been used extensively for state actors, is one of the defining characteristics of core companies. Bargaining power at the macro level is not new in relation to regional integration (cf. Balassa, 1961) but it has not yet been explored as a macro-micro issue.

3.2.5 Implications of the approach

Approaching regional integration as a level of analysis problem of strategic actors has limitations, and consequences. First of all, many of the concepts described in this chapter are ambiguous and difficult to operationalize. But given the tendency in economic models to assume ‘ideal-type’ behavior and uniform interests as well as assumptions of convergent patterns of behavior under institutionalization, there is a need for an approach that considers a wider range of strategic options, developing ‘strategic repertoires’ of regionalism. Further theoretical explorations at both the macro- and micro-levels will help to identify dimensions along which e.g. strategic intent and reality can be structured, and what the basis might be for the macro and micro strategic repertoires, respectively. Secondly, such an analysis requires a particular definition of regional integration. It requires a definition of regional integration that encompasses both political and economic elements, excluding e.g. purely military pacts like the NATO, constructionist approaches of e.g. perceived cultural convergence (Mansfield and Milner, 1997), as well as economic geography approaches and their emphasis on agglomeration effects, which may help to

explain different locations, 'but not different nations' (Dunning 1998, cited in Pitelis and Sugden, 2000).

Thirdly, the treatment of both macro- and micro-level actors as unified may be contested on the grounds that companies and governments are themselves much more than a cohesive group of individuals, and arguably the stage of interaction between multiple 'actors'. 'Reaction functions', by which observable outcomes are used to generate inferences about policymakers' intentions, offer little in analyzing policy (cf. Alt and Woolley, 1982). 'Finding a systematic means of relating intentions to outcomes is a serious problem of political analysis … We cannot just compare outcomes – this teaches us little if we do not take into account the intentions and the actions of the policymakers (ibid: 711). This means we have to distinguish between policy spaces where authorities have discretion versus those in which they are constrained. Although we run the risk of falling prey to the simplistic 'rational actor' approach of the optimization model, which portrays policy as being made by a unified authority with clearly defined preferences, it is, however, possible to typify the interests of a given firm or policymaking body such that each can be defined as a single actor *relative* to other actors. Any given firm (and similarly, an individual policymaking body) is characterized at some level by common overarching strategic interests that bind the 'group of individuals' in a way that sets their strategy apart from that of other actors (i.e., other companies). Otherwise the group would dissolve on the basis of its inability to define and pursue a shared direction.

Fourthly, defining and limiting the sample of actors is required to characterize the true nature of the 'small numbers game'. Conceptually it suggests on the one hand political actors whose behavior has economic consequences within the RIA context (e.g. the European Commission and the US Trade Representative), and on the other economic actors whose behavior has political consequences. Government actors and core companies will need to be more precisely defined. Finally, grouping actors at a given level entails the risk of oversimplifying their strategic realities, intents and behavior. Each level comprises different actors with different interests, and the categorization macro/micro is very broad. Still, the attempt is not to identify all the differences, but to identify the commonalities at each level and to show how, in a very broad sense, the levels can be so divergent that they cloud our understanding of the phenomenon. Creating a strategic repertoire concise enough to be manageable yet broad enough to capture a wider spectrum of possibilities will be a distinct challenge.

3.3 Regulation and economic restructuring

Since we assume that policy's greater institution-building and –enforcing capabilities give it a leading position in the macro/micro dynamic, it makes sense to look at the logic of regulation and assumptions of economic restructuring initially from a policy perspective. Doing so requires an assessment of the role of government in regulating political and economic behavior. Historically, there has always been a fit between the organization of economic activity (the regime of accumulation) and political institutions, behavior and belief systems (the mode of regulation) (Brodie, 1997). Numerous bodies of literature touch on these issues from a wide range of perspectives, including political science approaches like neo-Gramscianism and the 'Regulation school' as well as public choice and theories of the economics of regulation. This section begins by addressing recent developments in thinking on government policymaking (3.3.1), before examining views of

the government as one of a broader scala of stakeholders (3.3.2). This is followed by an historical overview of perspectives on the role of government in organizing economic activity (3.3.3). and an exposition of the spatial dimension of economic activity and its significance for policymaking (3.3.4). The section concludes by emphasizing the significance of the behavioral assumptions which underlie theories of government regulation (3.3.5).

3.3.1 The 'rethinking' of government policy

Mainstream theories of regional integration say little about *why* there is a second wave, and why this wave is occurring now. Generally, regionalism can be seen in the context of a broader 'rethinking of government policy' (Lipsey, 1997: 82) which emerged after 1975, when a new period of rapid structural change began. The main issues of structural change, both political and economic, are embodied in several key phenomena: the emergence of free-market thinking as the predominant economic ideology (with political consequences, the corresponding increase in interdependency, the increasing complexity of policymaking in the face of a larger playing field (horizontally) and multiple levels of governance (vertically), and the post Cold-War crisis of hegemony. These phenomena change the costs and benefits of given organizational patterns of structuring activity, and hence the costs and benefits of a given institutional context.

The past twenty years have been characterized by a 'doctrinal battle' (Lipsey, 1997), ending in the triumph of free market thinking and the pressures of liberalization, deregulation and privatization (Prakash and Hart, 1999). This ideology of the 'competition state' (Gill, 1994: 80) stands in stark contrast to the preceding protectionist period. The neoliberal ideology of free markets, as embodied by the Bretton Woods institutions (World Bank and IMF) and ideas propagated by supranational organizations like the OECD and the G-8, is rooted in a specific political philosophy (Scott, 1997). These institutions shape the discourse within which policies are defined (Cox, 1994) and are in fact ideological underpinnings, or even embodiments, of the dominant 'policy frame'. It should be noted that the free market does not mean an absence of government activity because even free market systems need rules and enforcement, but it does entail a reappraisal of the government's role as overseer of economic activity (Dunning, 1997b).

As free-market ideology predominates, economies become increasingly intertwined. Dunning (1997b) distinguishes in this regard between the extent of interdependency (effective boundaries of nation-states) and form of interdependence (degree and character of boundaries' porosity). This is also facilitated by technological developments that reduce the costs of communication, production and transportation (Lipsey, 1997; Strange, 1994). As transportation costs decrease, more and more goods are becoming 'tradables' (Gilpin, 2001). Increased transparency (Braithwaite and Drahos, 2000) also signals an increasing recognition of structural market failures. Disparities in economic growth or prosperity come more to the fore as economies are less and less isolated from one another. As economies become increasingly intertwined, national sovereignty may be challenged by increased exposure to destabilizing factors like capital flows and interpenetration of markets by foreign firms (Gill, 1994). Dunning (1997b) calls this the increasing ease with which competitiveness-enhancing assets can move across national borders. Given that these assets are often the property of an ever-diversifying body of companies from different national backgrounds, governments are faced with an increasingly complex range

of interests. The spatial boundaries of nation states and the significance of location-specific advantages of countries need to be reconfigured as government policies are increasingly affected by the policies of others (Dunning, 1997).

Increased transparency and the compression of time and space amounts in a sense to a crowding of more and more jurisdictions, or governance structures (Prakash and Hart, 1999). Growing interconnectedness means that actors are increasingly exposed to a wider range of potentially fundamentally different governance structures (horizontally). As problems become 'bigger', states are forced to delegate authority (vertically) to supranational entities (Lake, 1999). Braithwaite and Drahos (2000) refer to this as the 'globalization of rules'. Regulatory power is being situated in new locations (e.g. Brussels, GATT) that overlap, supersede and sometimes contradict preexisting (national) domains in geographic space. The implications can be far reaching; Strange (1995) claims the state is 'hollowing out'; governments are the victims of a shift in the state market balance of power. Lake (1999) adds that there are large, unclaimed political spaces in the international arena amidst the 'mishmash of rules' (Graham, 1997: 500), which at least to some extent have been filled by large corporations (Prakash and Hart, 1999). Ohmae (1990) and others even go so far as to suggest that additional layers of policy complexity and governance structures signal the end of the Westphalian nation-state.

In the bipolar world that preceded the fall of the Iron Curtain in 1989, there was a higher degree of certainty with respect to political allegiances and spheres of influence. Largely as a response, the geopolitical positioning of numerous nation states has shifted and changed (e.g. the former Warsaw Pact countries), and in some cases countries have disintegrated completely (e.g. Yugoslavia). A much wider range of countries has experienced rapid economic and/or political transition in the same period. Fragmentation of the Cold-War institutional constellation has ushered in added uncertainty for policymaking in the international arena and contributed to a slowdown of the multilateral process. That uncertainty can be linked to a diffusion and decentralization of institutional power back to the national and regional level (bloc-formation) while the market continues its climb to an increasingly global level, signaled by a shift in the international agenda towards economic issues (Leaver, 1994). This fragmentation, however, has played a large role in the difficulties surrounding the development of a broader multilateral system, with the rise in regionalism as an inevitable result (Baldwin, 1993). Bhagwati (1993) refers to this phenomenon as a shift from rule-based international relations back to power-based international relations. The tension between these tendencies creates an additional level of complexity for policymakers.

3.3.2 Configurations of institution-building

The changes taking place in the technological, economic and geopolitical spectrum have an impact on the configurations of social actors within which new institutions are formed. These 'configurations of institution-building' encompass the bargaining environment, and describe the interplay between the key actors which shape regulation, also known as the 'nexus of stakeholders' (Van Itersen and Olie, 1998). Whereas older schools of thought emphasized the homogeneity in social organization ('pluralist industrialism'), 'new institutional' theories emphasize the diversity in institutional structures between societies (Crouch and Streeck, 1997) and the differences in interaction between societal, economic and political actors. The analysis of recent upheaval in forms of the organization of

production has been seen in the context of the crisis of post-Fordism (Boyer, 1997; Bakker and Miller, 1996; Ruigrok and Van Tulder, 1995; Piore and Sabel, 1984; Aglietti, 1979).

Configurations of institution-building are used in this sense to follow up on the Fordist debate to describe the processual link between government regulation and the activities of economic actors. These configurations are defined by the number and relative influence of stakeholders organizing production, such as business interests, labor (trade unions) and other societal actors, and particularly the role of the state (Martin, 1994). The role and influence of stakeholders is in turn a question of the 'social embeddedness' of economic institutions (Jessop, 1999). Such configurations can also be viewed as 'concepts of control' (Ruigrok and Van Tulder, 1995). Concepts of control refer to long-term strategies for solving five key control dilemmas: the labor process, the supply of components and raw materials, distribution and consumption, core production technologies, and finance. Although firms and banks are proactive in this process, there is also "the *role to be played by the state*, including a definition of the 'national' or 'common' interest" (Ruigrok and Van Tulder 1995: 38; italics added for emphasis).

Such configurations are generally analyzed at the national level (Crouch and Streeck, 1997) because 'policy space' at this level is generally supremely sovereign. The national foundations of the spatial organization of economic activity is the subject of a large body of literature on 'national systems of political economy' (Gilpin, 2001),'national systems of innovation' (Lundvall, 1992; Nelson, 1993; Porter, 1990), 'production regimes' (Wilkinson, 1983; Rubery, 1994) and on 'national business systems' (Whitley, 1992). The literature on endogenous trade theory also focuses on the motivations of policymakers and domestic interest groups in the shaping of trade policy (Baldwin, 1985, Caves, 1976). This means that configurations of institution-building center on domestic actors and their pressure activities. In other words, the establishment of concepts of control, or modes of regulation, is a product of the *domestic bargaining environment*.

The post-Fordist model emerged out of the work of French regulationists, most notably Aglietta (1979) and Lipietz (1987). They argue that the crises of the 1970s and 1980s signified a breakdown of the prevailing Fordist political economy, which was characterized by mass production technologies, a mass consumption culture, and Keynesian welfare policies. Regulationists view Fordism in a wider perspective of capitalist development as a sequence of internationally different historical formations that evolve through crises and conflict. In situations of crisis, social actors are forced to abandon established norms of behavior and to develop new strategies to deal with the crisis. Their strategies reflect different interests, different visions of the roots of the crisis, and thus different options on how to deal with the crisis; hence, strategies may be conflicting. Economic institutions are formed through the compromises made between these divergent interests and as such differ from the classical market-effectiveness approach.

Macroeconomically, there may be a new articulation of modes of production, called a regime of accumulation (Boyer and Durand, 1997). According to regulationists, each stage of capitalist development consists of a particular regime of accumulation and mode of regulation. The post-Fordist regime of accumulation is driven by new information technologies and organizational networks. The regime of accumulation requires a set of fitting explicit and implicit rules and norms for its stabilization, called the mode of regulation. This involves state, money, wage relations and modes of competition. Aglietta differentiates between two types of regime: Keynesianism and productivity coalitions,

linking wage increases to labor productivity; and Monetarism, or supply-side economics, in which variable capital (wage goods) are rendered more cheaply. Either type will eventually reach its limits in the domestic market and require an 'extraversion' of accumulation strategies. This is nothing less than the internationalization of a mode of regulation under the auspices of the government; in other words, the internationalization strategy of the state.

Fordism can be subdivided into micro-Fordism or macro-Fordism (Ruigrok and Van Tulder, 1995). 'Macro-Fordism' entails the simultaneous growth of production and consumption generated not only at the firm level, but also at the societal level, 'involving actors such as governments and national trade union federations' (ibid, p. 12). In other words, macro-Fordism, also called tripartitism, (neo)corporatism and statism (Schmitter, 1974; Cox, 1989) entails a centralized bargaining environment operating at all levels. In a micro-Fordist system (see also Strange's 'crony capitalism'), the state is highly centralized but non-interventionist, resulting in low levels of cohesion with business (Lane, 1992). The emphasis in economic organization is therefore at the firm level. Different post-Fordist orders have been suggested in the literature, predominant among them Toyotism, Uddevalism and flexible specialization (Boyer and Durand, 1997; Piore and Sabel, 1984).

The Toyotist concept of control refers to centralized *indirect* or *informal* control over external supplier markets, shorter production runs, domestic innovation, indigenous technological know-how and autonomous industrialization (Van de Gevel, 1997). Toyotism is characterized by close cooperation with government as opposed to confrontation (Ogata, 1999). Japan, with its 'weak state' (Ruigrok and Van Tulder, 1995) and history of close business government relations (Van de Gevel, 1997) is the prime example of a Toyotist environment. Flexible specialization is a vision of small, flexible and highly networked firms operating on the cutting edge through 'a strategy of permanent innovation: accommodation to ceaseless change, rather than an effort to control it' (Piore and Sabel, 1984: 17). Uddevalism (derived from the name of a Volvo factory in Sweden) is actually only a theoretical basis for a production model in which the division of labor is radically reorganized through elimination of the assembly line, such that workers have much more power over machines and production, combined with a national-level capital-labor compromise (Boyer and Durand, 1993). The variation among these regimes suggests that there is not necessarily a universal strategy for addressing post-Fordism.

Whatever its form, core companies, particularly those with cross-border activities, are an integral part of the emergent post-Fordist order. They are the answer to the problem of microeconomic regulation. Core companies rely upon factories located around the world to produce parts that are later assembled in one locale. They increasingly rely upon subcontractors, part time labor, just-in-time inventory systems, and other information technologies to minimize costs (Dicken, 1992). Cost minimization, however, often leads to cost externalization, as workers and ecosystems are exploited to bolster profits (Foster, 1994). Brecher and Costello (1994) and others argue that post-Fordism has initiated a "race to the bottom". Free-market ideology embodies a new growth regime, or mode of regulation, based on cost minimization, price mechanisms, intellectual property rights, open economies and productivity growth in which core companies play a key role. Other supranational arrangements such as RIAs as well as the World Trade Organization (WTO) are suggestive of a new global mode of regulation designed to facilitate the post-Fordist regime of accumulation.

Configurations of institution-building mean that political actors are not free to do as they please. Rather, much like the strategy feedback loop described in section 3.1, they are limited by 'a historically specific field of constraints imposed by, among other things, international power structures and the force of previous decisions' (Brodie, 1996: 383). In the changing context of international policy strategies, regionalism may be part of the emergent post-Keynesian and post-Fordist order, first and foremost because concepts of control, but also competitive space, are determined less and less in domestic bargaining environments and policy spaces, and more so in an internationalized operating environment.

3.3.3 The role of government in organizing economic activity

Although Dunning (1997c) describes governments as simply one mode of organizing activity (beside markets, hierarchies, intrafirm alliances), Chang and Rowthorn (1995) argue that state involvement is in any case required for the establishment of a *new* coordination structure. The state is the only entity able to legalize and give backing to the new relations of power which provide an *institutional reality* to the new structure. The state is also the only actor which can more or less represent the broad spectrum of interests in the society as a whole. Chang (1994) describes the role of government as 1) creator and sustainer of institutional, legal and commercial infrastructure, 2) fashioner of value systems and ideologies, 3) provider of focal point around which allocative decisions can be coordinated, and 4) as the provider of a vision of the future. These are the 'economic-productive' activities of political governance; the realms of coercive-protective and social-communal governance (McGinnis, 1999) are not addressed here.

State entrepreneurship does not stop at the provision of a vision of the future. If this vision is to be implemented, the state has to provide an institutional reality to it. This means looking at the state in the role of *institution builder* (Chang and Rowthorn, 1995: 37; original italics). It is the government's responsibility to establish consensus, in the sense of convergent expectations among actors, and not necessarily in the sense of a harmonious process (Chang and Rowthorn, 1995). States have to enlist non-state actors (often with different preferences and endowments) in institutional design and implementation in a process of 'rearticulation' (Prakash and Hart, 1999: 15). In building institutions for the organization of economic activity, the government is also a process manager, facilitating the interaction of other stakeholders. Similarly, government can be seen as a market maker, linking 'supply' and 'demand' for policy interventions (Mattli, 1999a).

Visions of the government's role in organizing economic activity differ depending on the overall view of how the economy functions. In free-market ideology, states provide public goods of law and order, sound money, regulation of markets, and protection from invasion, acting as it were as a benevolent nightwatchman (Gill, 1994). This entails an emphasis on market failure, and a tendency to think that less intervention is better than more (Dunning, 1997c). The degree to which intervention is acceptable depends on the issue being addressed, e.g. whether the focus is unemployment reduction, social reform, national competitiveness or environmental concerns. Additionally, organizational strategies depend on the kind of market that exists, often related to sectors – in the case of agriculture, for instance, intervention is much more widely accepted than in manufacturing.

An explicit philosophical view on the state's role in organizing economic activity started with Mercantilism, which argued that the political needs of the state should be served, not

the needs of economics. Similarly 'less enlightened' motives for intervention can be e.g. paternalism and self-interested redistributive behavior (Lipsey, 1997) or the desire to maintain political power (i.e., re-election) identified by public-choice theories (Grossman and Helpman, 1994). The French Physiocrats responded with 'laissez faire' as the 'natural' order of things (Dunning, 1997c: 38), which was in turn countered by welfare economics, pioneered by Arthur Pigou, largely as a reaction to the social issues that were raised by the Industrial Revolution (Chang and Rowthorn, 1995a). Welfare economists argued that free markets may not achieve a socially optimal resource allocation and that government manipulation of price mechanisms could therefore be justified. This line of thought led to theories of state-led development policies developed by Raul Prébisch and Nicholas Kaldor.

More recently, classical economic thought has generated the cost-benefit view, emphasizing rational behavior, perfect markets and Pareto optima. Government exists to counter five major market imperfections (cf. Dunning, 1997c): structural distortions that inhibit competition; endemic market failures due to intrinsic market impurities, like externalities which cause divergence between private and social welfare; the issue of structural unemployment; and lastly the transaction and coordination costs of economic organization (as opposed to the production and transformation costs), meaning in essence the furnishing public goods. North and others argue that transaction costs are increasing and that in this sense the role of government may need to increase. Additionally, there are processes of technological and organizational change identified by Schumpeter (along with Kondratieff), who argued that innovation was the main driver of economic change. He believed that technological progress would lead to 'instabilities in production and exchange, demand new organizational structures, and encourage more influential governments' (Dunning, 1997c: 51). In other words, even in a free-market system, the role of government (not its absence) is crucial, and assumptions of perfect competition, price signals and optimum resource allocation say nothing about an economy in which change is endogenous and path-dependent (Lipsey, 1997). Fundamental to all the aforementioned perspectives, however, is a recognition of the costs of government intervention.

3.3.4 The macro-reality of location

Economic change is endogenous because political actors' decisions have economic impact. In other words, issues of economic organization are where policy space and competitive space overlap. Why is the location of economic activity relevant from a macro point of view? Because the locus of (value-adding) activity determines policy-relevant indicators like terms of trade, growth levels, and the rents which accrue (e.g. in the form of taxes on goods, wages and profits, which in turn has an impact on sovereignty, policy jurisdiction and ultimately the legitimacy of the state. Traditionally the best way to achieve this has been to produce goods from the home country (or the relevant policymaker domain), and export to external policy domains. This generates improvements in terms of trade and the balance of payments, tax revenues and has a positive effect on jobs and production (Vernon, 1993). Jovanovic (2001), on the other hand, argues that the logic of trade (based on Ricardo), is a matter of exporting as *a means to finance imports*, not as a means in itself. But this is only a perspective of consumer welfare. The issue is more than just trade, and also more than the range of selection the consumer has when shopping; put simply, the macro-reality of economic activity concerns the rents generated by location of value-added

activities. Additionally, inward and outward investment affects factor endowments and factor demand, which has an impact on government competitiveness and 'systemic' power. From a policy perspective, governments want to 'host' economic activity, and hence the macro-reality of location is a question of attractiveness to economic actors. This applies in particular to core companies, given their 'flagship' function among competitors, suppliers and customers as well as their intangible assets (tacit knowledge, production techniques, core technologies). In the past this competition for foreign investment was viewed with considerable scepticism, since foreign capital was often perceived as a threat to local industry as well as to the bargaining power of the host government (Lipsey, 1997; see also Guisinger, 1985). The macro-reality of economics centers on spatial inequality (Schwartz, 1994). Spatial inequality is 'explained' by numerous theories based on diverse assumptions, including neoclassical economics, Von Thünen rings, world-systems theory and dependency theory. Neoclassical economics essentially argues that spatial inequality is a result of varying supply and demand curves for production factors, while Von Thünen's argument links the relative price of goods and production factors with the distance to market (Jovanovic, 2001; Schwartz, 1994). Dependency centers on 'core' economic areas and the forced dependency of peripheral regions (i.e., the underdeveloped world) on the economic demands of the core, while world-systems theory argues that underdevelopment is not solely a by-product of capitalist exploitation.

Distinctly political matters of government like security and order are, especially since the Industrial Revolution, increasingly dependent on development levels and economic growth (Panić, 1995). Mokyr (1990) distinguishes three sources of growth: 'Solovian' (capital accumulation), 'Smithian' (expansion of markets) and 'Schumpeterian' (technological change). Schwartz (1994) adds an international dimension to growth strategies by distinguishing between Ricardian (trade-based) and Kaldorian (investment-based) growth strategies, with the emphasis in recent times on the latter, particularly in developed economies. Although governments are seen as actively vying for foreign investment to serve their development objectives, investment is primarily directed at highly developed economies (Encarnation and Wells, 1986), which suggests that the stimuli for investment in developed countries are already present, possibly in the form of the capacity for innovation (Lipsey, 1997).

A key concern for governments is the possibility that core companies might relocate, particularly in response to the policy inducements of other governments ('location tournaments'). Governments have a dual nature: on the one hand promoting, on the other hand protecting against global competition (Porter, 1986). Governments are interested in protecting infant industries (Doz, 1986) and also enjoy the revenues generated by import tariffs. To show that competition in policy space differs from competition in competitive space is the fact that the major competitors of US firms are other US firms (Gilpin, 2001). Policy-induced market distortions, like restrictions on either products or on factors of production are government creations intended to somehow protect domestic input or output markets (Wartick and Wood, 1998). States have incentives to promote firms closely associated with their territorial jurisdictions (policy space), a phenomenon known as 'commercial diplomacy' (Prakash and Hart, 1999). In competing for locational attractiveness, governments can play off firms against one another, but firms can do the same; at the same time, firms try to front-load incentives, while governments try to stretch them out (Doz, 1986). Location, therefore, has implications for the balance of power between states and markets, and configurations of institution-building. Location influences

the emergent configuration, and the configuration influences location, forming yet another strategic feedback loop.

3.3.5 Assumptions of political behavior

Policy preferences are rooted in perceptions of political behavior, or, to paraphrase Stephen Gill (1994), 'theory is always for someone and for some purpose'. The most important distinction in political theory is between realism and idealism (see Gilpin, 2001). Realism is very much associated with the state-centrist view of the likes of Machiavelli, Morgenthau and Bismarck. Neorealism (Waltz, 1979) takes a more holistic view in which the distribution of power *among* states is key instead of the state's interest in itself. The underlying assumption is that the world system is anarchic, not in the Hobbesian sense but such that no higher authority than the state exists to arbitrate in international affairs. Idealism is based on John Locke and reflected in e.g. Woodrow Wilson's League of Nations, which had as a premise that nations could work together to solve collective problems in the interest of all. In the Lockean state of nature there are no institutions, only agents, preferences and technology to convert inputs to outputs (Schotter, 1981). Institutional development is a 'social contract'; institutions evolve through human action but not necessarily through human design. Idealism has been less favored than realism since the Second World War (Keohane, 1984).

More recently idealist thought has been superseded by 'liberal' views of politics, which take a more economic perspective of politics and are concerned with the freedom and welfare of individuals. Although liberalism can be seen as a variant of realism if individuals are assumed to be self-interested, liberalism is actually idealist in the sense that it assumes human beings can develop harmonized interests through rational behavior. From a practical point of view, altruism may exist simply because individuals' respective interests are mutually dependent, but Phelps (1975) argues that we should also consider the possibility of acts of altruism based on a generalized regard for human rights, social codes, business ethics and so on (cited in Baldwin, 1985). Unlike realism, then, liberal perspectives treat economics as an area of concern in its own right instead of relegating economics to a matter of politics (security). Economics is then very much a vehicle for increased cooperation between states, and free markets yield the greatest good to all.

Ideas about behavior are also rooted in the era in which they are propagated. Realism has lost some if its allure because of the increasingly multilateral character of some aspects of the international order, such as the UN and the myriad of international conventions governing international politics and economics. Idealism is more associated with in particular economics-oriented approaches that attribute benevolent characteristics to the international economic order. In idealist approaches, political behavior is rational or consequence-driven, meaning individuals assess the costs and benefits prior to action (McGinnis, 1999). The state recedes to the background and has only a facilitative role in ensuring the optimal functioning of the market to the end of welfare optimization. To a certain extent the idealist/realist dichotomy is one of prescription versus description, normative versus positive, or 'soll versus ist'.

Yet to assume away the strategic behavior of governments is naive and unrealistic. Realists criticize such assumptions, arguing that behavior is more complex and much more than an action based on a cost-benefit analysis. In fact Krasner (1978) recognized that a delimited set of policy preferences emerges over time, which is in fact recognition that past strategic

behavior conditions the range of strategic options in the present (history matters, and behavior is to some extent path dependent). Sandholtz (1999) asserts that actors have interests or goals only in the context of social relations that produce shared meanings and values (Prakash and Hart, 1999). Thus, institutions are more than bargaining forums where utility maximizing states with autonomous preferences construct arrangements for minimizing transaction costs. Actors make decisions by analogy and not by cost-benefit calculations. Decisions depend crucially on beliefs and values and how issues are framed (Prakash and Hart, 1999; Dudley and Richardson, 1997).

3.4 The choice of regionalism strategy

The perception of strategic intent, given its emphasis on the expected behavior of other actors, can be related to realist or idealist assumptions of behavior, in particularly notions of communal interest versus self-interest. It can be acknowledged that regionalism by its very nature has more of a realist approach because it assumes strategic behavior as a means to gain something, without the assumption, implicit or explicit, that those gains will accrue to all (not even all regional parties). The very notion of strategic behavior indicates on its face a realist-type approach, but still recognizing the need to take economics into account as more than just an issue of security. The assumption that state interaction in the international system is by its nature anarchic is acceptable, but the neoinstitutionalist assumption must be recognized that supranational institutions have a role in defining the strategic options (as 'intervening variables') available to governments (Cameron and Tomlin, 2000). Finally, the concept of multi-level games is revisited to emphasize the role of international *and* domestic interests in shaping international policy preferences at the government level.

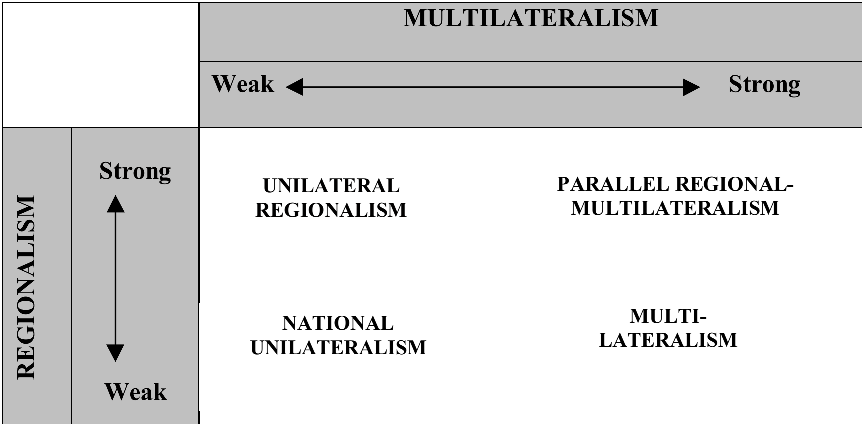
3.4.1 Three 'isms' and internationalization strategies of the state

Regionalism strategies cannot be considered in isolation or as exogenous shocks; rather, they are best seen in the context of the wider debate of alternate 'modes of regulation' in the global economy. These modes of regulation consist of more than just multilateralism, which could be presented as the mode of regulation of 'globalization' in the context of the debate in 2.5.3. If regionalism is characterized as a mode of regulation in the context of state internationalization strategies, it must be recognized that there are other strategic options. Since national governments remain the most ubiquitous sovereign policymaking bodies, unilateralism must be taken into consideration as well. In theory, governments also have the option to 'go it alone' (Lung and Van Tulder, 2004), pursuing neither regional nor multilateral strategies. Unilateralism means that states retain the right, and sovereignty, to pursue their own interests, regardless of the interests of other states. Regionalism is internationalization of the state within a 'club' framework, and multilateralism is full commitment to the neo-liberal ideology of market liberalization. In this sense regionalism is more than a description of policy choices; rather, it is an ideology as well. The three may seem mutually exclusive as ideologies, but as internationalization strategies of the state, they can be complementary.

Figure 3.6 demonstrates how unilateralism, regionalism and multilateralism can be related conceptually. In the 'regionalism vs. globalism' debate the dichotomy is between the pursuit of state internationalization strategies primarily through multilateralism ('strong'

multilateralist and 'weak' regionalist tendencies) or through 'unilateral' regionalism ('strong' regionalist and 'weak' multilateralist tendencies). On the other hand, it is possible that a government pursue both multilateral and regional institution-building in a parallel, mutually reinforcing strategy. Finally, it should not be forgotten that states can adopt an autarkic stance of 'national' unilateralism, where both regionalism and multilateralism are avoided. Unilateralist strategies with respect to trade liberalization are particularly associated with developing countries in the 1980s (De Melo *et al.*, 1993).

Figure 3.6: Regionalism, multilateralism and unilateralism



Source: Based on Lung and Van Tulder, 2004

The framework in Figure 3.6 remains conceptual in the sense that it makes no attempt to explain the likelihood of one strategic choice of the other, nor how multilateralism, regionalism and unilateralism should be measured empirically. The strength of a government's multilateralist tendencies could be measured by involvement in WTO and adherence to IMF and World Bank principles. States will use whichever suits their interests, and these interests, and therefore strategic choices, can change over time. Changes to these preferences can be cyclical, related to hegemonic cycles, or long waves, and must be seen in the context of a government's strategic reality.

3.4.2 Policy strategies and three tiers of interests

It was argued in section 3.2 that an actor's strategic reality conditions its preferences, and is largely shaped by previous behavior and behavior expected of others. Traditional International Relations literature tends to view regionalism strategies in the international context, with national interests as essentially a predefined given. Since nation-states are the key actors in international politics, they form the primary unit of analysis. In this section a state-centric view of conflict is also adopted in order to bring the logic of policymaking to the fore. Yet other actors both inside and outside the nationally defined policy space also have (potentially conflicting) preferences, which affect the preferences of the national government. National policy preferences, and thus strategic choices, can be seen in terms

of the domestic bargaining arena (the national level), or in terms of the interaction with other (potential) regional member states (the regional level). Equally valid is the contention that regions can operate as actors on the international stage, and therefore have shared preferences relative to other regions or individual countries (the supraregional level). Relationships between actors in terms of perceived interests can therefore be analyzed at multiple levels (Table 3.1). Whether relationships at various levels are seen as harmonious or adversarial will condition policy preferences.

Table 3.1: Three tiers of interests in policymaking

Level	*Focus of policymaking*	*Perceived relationship*	
		Harmonious	*Adversarial*
Supraregional	Regional blocs	Building blocs as a manageable step towards an open, interdependent multilateral system	Stumbling blocs entrenched in inter-regional competition
International	Intergovernmental bargaining arena	Solving collective action problems through the joint provision of public goods	Institutionalization of rent-seeking behavior; exploitation of power asymmetries, me-too strategies
National	Domestic bargaining arena, in particular core companies and their webs of stakeholders	Serving domestic business interests through protection, reduction of uncertainty and transaction costs	Pressure core companies by restructuring the bargaining arena and altering competitive space

The categorization of behavioral assumptions into idealist and realist behavior (addressed in Section 3.2.2) is rooted in perceptions of relationships between actors. The idealist perspective essentially assumes that individual actors can define shared, harmonious interests by which each actor gains. Harmonious is another way of saying altruistic when welfare or interests of the one depend on the welfare of another (Baldwin, 1985). Realism takes as its point of departure the assumption that interests are adversarial, although it is not impossible for actors to 'coincidentally' share preferences. Furthermore, the interests and identities of actors are defined through interactive processes (Cameron and Tomlin, 2000). This also makes them relative, in that preferences are not predefined but emerge through these interactive processes and are seen only relative to other strategic options (cf. Krasner, 1982). Perceptions of harmonious and adversarial relationships should be seen in this relative sense and not absolutely.

Although it is theoretically possible to perceive relationships as harmonious or adversarial at all levels, in practice, and with respect to specific issues, each level is best considered *relative* to the other levels. As such, one particular level of adversarial relations (conflicting interests) will emerge as the focus of policymaking tension. This is essentially a realist / regulationist argument because it rests on the assumption that preferences are not just based on static, predefined interests, but that they emerge from areas of (perceived) conflict. If a government, for instance, sees the domestic bargaining environment as the focus of conflict (e.g. adversarial relationship with home core companies), it may seek cooperation with other states (regionally or multilaterally) as a means to resolve the conflict. Similarly, if a government sees other states as the primary source of conflict, it may focus on engaging domestic stakeholders as allies in defending the national interest (unilaterally). If the government sees a limited number of states as potential allies (regionally) with shared interests relative to other states or groupings of states, it may engage in 'unilateral regionalism'. The choice depends on the number and characteristics

of stakeholders the actor is involved in. Countries with complex and extensive network of intergovernmental relationships may have perceptions of conflict at multiple levels across different issues. It is also progressive (dynamic) because groups of states with shared interests can increasingly be perceived as 'unitary' actors.

The preceding arguments link the post-Fordist debate (national relationship with labor and capital; in this case core companies) with realist and neoinstitutional theories of state (and regional) interaction. Fordism represents the perception of harmonious interests at the national level. In policy terms, this is translated into e.g. high subsidies to companies, the development of infrastructure, credit policies favorable to investment and public spending designed to moderate cyclical fluctuations (Boyer and Durand, 1993). Panić (1995) looks at the degree of economic consensus, both nationally and internationally, as a factor which determines the effectiveness of policies, and thus institutions. The lobby function discussed with respect to core companies (section 3.1.3) is fundamental in this regard. This brings us back to the interactive feedback loops (section 3.2.1) because it shows that firm efforts to influence policymakers and policymaker expectations of firms influence the course of international policymaking and institution-building. Thus regionalism is a three-level game, with domestic interests (core companies), intergovernmental bargaining, and the impact of extra-regional dynamics on the definition of regional interest. Key, therefore, in identifying the issues shaping regionalism strategies is to identify the main level(s) of contention.

Furthermore, these options can be related to the origins of regionalism found in the literature and discussed in Chapter 2 (Table 3.2). The literature suggests a wide range of domestic and foreign policy-driven motives for regionalism strategies. These motives, while not necessarily mutually exclusive, can be conflicting, and thus pose strategic policy dilemmas for governments. It would be presumptuous to suggest a definitive 'unitary' driver of government behavior; rather, it is argued that all the theoretical 'origins' discussed above can be applicable, depending on the degree of perceived cohesion between actor interests at the domestic level, between nations, or even between regional blocs.

Table 3.2: Levels of conflict and policy strategies

Focus of conflict	*Internationalization strategy*	*'Origin' of Regionalism*
Interregional bargaining arena	• Unilateral regionalism	• Collective action problems e.g. reduced transaction costs (under pluralism!)
	• Multilateralism • Parallel regionalism-multilateralism	• Maximization of national power through 'building block' (the hegemon)
Intergovernmental bargaining arena	• Unilateralism	• Domestic demand for protectionism • Maximization of national power
	• Unilateral regionalism	• Defensible multilateralism • Maximization of national power through 'stumbling block'
National (domestic) bargaining arena	• Unilateral regionalism • Multilateralism • Parallel regionalism-multilateralism	• Pressure domestic stakeholders; also with other governments as a collective action problem

If the domestic bargaining arena is the main locus of tension in policymaking, regionalism and / or multilateralism may be useful strategies because it allows for leveraging the

weight of a larger political entity (e.g. regional members, the WTO) in forcing through reforms (the 'lock-in' option). If governments see relative cohesion at the national level, but perceive themselves to be predominantly engaged in competition with other states, they may adopt a unilateralist position, either in response to domestic demand (often for protectionism) or as a strategy of national power maximization (through minimal sovereignty concessions). On the other hand, even under conditions of perceived conflict, a government may choose to opt into an RIA as a form of defensible multilateralism as a 'least risk' strategy, or as a strategy to enhance national power by limiting the progress of multilateralism (facilitating the 'stumbling block'). The third possibility involves shared interests with a select number of other governments, and perceived conflict with other states or clusters of states (e.g., regions). In this case strategies can be inward or outward in orientation. The former essentially encompasses collective action problems, such as the reduction of intra-regional transaction costs and coupling supply and demand at the regional level. The latter involves the use of regionalism as a stepping stone towards multilateralism, which allows the government (through the weight of the regional grouping) to have extra influence in determining the future shape of multilateralism. Additionally multilateralism can be employed selectively as a flanking strategy to undermine the strength of other regional groupings.

3.4.3 Positioning in choosing a regionalism strategy

How perceptions of conflict at various levels are related to specific strategic issues facing governments, and how these can lead to the initiation of RIAs is beyond the scope of this study. However, it can be argued that perceptions of conflict are related to issues of power and strategic positioning which do have a direct bearing on the decision to regionalize, and the decision as to what *form* of RIA to undertake (e.g., a PTA or a CM), and how the relevant policy mechanisms (see section 2.4) can best be implemented. Since strategic behavior with respect to regionalism is based on an actor's strategic reality (positioning) as well as expectations of other actors (other governments as well as core companies), perceptions of conflict are relevant. Perceived levels of conflict are related to relative development levels, market power and hegemony, and pre-existing economic and political relations (i.e., the outcomes of previous strategic positioning behavior).

First of all, it can be argued that the level of perceived conflict is fundamental in limiting the extent of policy cooperation, or the depth of integration. This means that governments involved in an adversarial relationship with the interests of big business will have more difficulty engaging in extensive policy cooperation with others, even though they may see it as in their interest to do so (pressuring domestic stakeholders through 'lock-in' strategies etc.). In other words, invasive and costly exercises of 'deep' integration, like a common market or a monetary union, are only feasible if there is enough of a shared vision between government and core companies at the national level as well as sufficient 'critical mass' among a number of like-minded governments at the 'regional' level.

There is considerable disagreement on the relationship between internal cohesion / conflict and international bargaining strategies. Cameron and Tomlin (2000) argue that the perceived level of harmony between domestic interests and government (internal cohesion) is in fact a *by-product* of a country's relative international bargaining power. Their argument is that powerful states have more room to listen to their domestic constituents than weaker states, which are forced more to cater to outside influences than press their

own domestically-driven agenda. This is dubious, because their underlying assumption is that the government prefers not to engage in supranational cooperation for fear of having some 'weakness' exploited, whereas in this particular case it is argued that the government *wants* to employ a regionalism strategy *precisely* for the purpose of undermining the position of (adversarial) domestic stakeholders. Harmonious interests at the national level have in this sense bearing on the strength and the character of regionalist tendencies. Others argue that internal divisions may be an asset because negotiators can stall and smokescreen on the international bargain, and then argue they 'couldn't get more' concessions from their constituents (the 'Schelling conjecture'; Meunier, 2000). Milner and Rosendorff (1997) argue otherwise, claiming that internal divisions among domestic stakeholders make ratification less likely, tilt the outcome towards protectionism and weaken the country's negotiating power relative to other countries.

The political theories reviewed here use the two levels of Putnam to make their case, i.e. the executive (the international negotiator) and legislators (responsible for ratification). Yet the overemphasis on politics in these studies makes them weak for our purposes. It can be argued that adversarial relations between government and domestic interest groups, in particular core companies, will weaken that country's bargaining power because, unlike in the case of legislators (the domestic level in Putnam), core companies have more power in shaping the *restructuring* outcome after the implementation of the institutional outcome (the international 'bargain', in this case an RIA). For bargaining partners (other governments), power of this nature has a different significance, because core companies have direct disposition over the allocation of economic resources, much more than legislators do. Additionally, the consequences of core company allocative power are farther reaching, because the life-span of the average core company (see Van Tulder *et al.*, 2001) is considerably longer than the term in office of the average Congressman.

International restructuring processes (and therefore regionalism strategies) are games of strategic positioning between governments and domestic stakeholders, between states, and even between regions. In international negotiations, 'market power remains the basic prerequisite to gaining concessions' (Canadian NAFTA negotiator Michael Hart, quoted in Cameron and Tomlin, 2000: 15). Strategic positioning is a question of power, but power does not stem solely from harmonious relations with domestic interests. Market power concerns positioning relative to other countries, which is for instance also related to development levels. One of the 'new' aspects of the recent wave of Regionalism is that it is not specifically a developing country phenomenon. The emergence of RIAs between countries of disparate development levels must to some extent be a factor in the increasing complexity of policy strategies. The degree to which a policymaker disposes over resources will affect the strategic intent, and thereby determine the outcome, of a regionalism strategy.

Mattli (1999b), for instance, suggests that lower growth levels will stimulate any given country to seek membership in a preexisting region. His argument is based on the prospect of free-riding, but it is also valid in that economically weaker countries will have more difficulty initiating a new RIA because they lack the political weight to pull it off. There is also a more economic rationale drawn from his 'supply and demand' argument: the more well-off a nation is, the lower the relative gains that can reasonably be expected from integration. On the other hand, there may exist a minimum level of prosperity required for integration, since countries without much to trade or without developed markets will stand little to gain from integration in economic terms. Winters (1999) claims that *disparities* in

development levels are crucial to the choice of regionalism strategy. He argues that in cases of North-South integration (i.e., NAFTA), the central issue pertains more to attracting investment to the developing partner than trade, and that investment in the South is a stabilizing factor from which the North also benefits. Development issues, such as Ethier's (2001) terms of trade sensitivity, have to do with how sensitive or vulnerable a country is to the actions of others.

The arguments above suggest that a country's power, be it market power, military power or systemic power, should be seen *relative* to the countries with which it interacts; in other words, a country's position in a larger constellation of economic activity will largely determine its bargaining power. That constellation is finite and unique to each country, as opposed to the notion that each country is positioned relative to some static median or the 'rest of the world' as a whole. Not all countries 'do business' with all other countries. Bargaining becomes a question of relative political asymmetries (Cameron and Tomlin, 2000) within a country's specific geopolitical network. This returns to the question of hegemony versus political pluralism (cf. Wartick and Wood, 1998). Mattli (1999b) and Van Tulder and Audet (2004) look at this as an outcome (see section 2.4.1), when in fact it is equally relevant, if not more so, to consider power asymmetries (and related information asymmetries) as a factor in *determining* both the institutional and the restructuring outcome. Whether regional integration can only occur in the absence of a 'global' hegemon or not is immaterial; the fact is that regions themselves may be dominated by a *regional* hegemon.

Mattli (1999b) argues that uncontested regional leadership increases the chance of success, combined with relative potential market gains from integration, and that an 'absence of leadership' can cripple a region. His argument suggests that a 'hub and spoke' constellation in a region will be the most successful. Dent (1997) in essence supports this view, stating that an RIA will be more successful if one of the members is already a major trading power, and that the international bargaining power of the region will profit from such membership. In addition, it will attract new members (like Austria and Sweden in the case of the EU). Yet Haggard (1997) talks of political and economic heterogeneity as being a barrier to integration. If a region is dominated by one or more power, the contents of the agreement may be more a reflection of their interests than of the other members. The me-too strategies of countries feeling left out, or as a strategic complement, are examples of strategies determined largely by the policy preferences of others. Regionalism under a hegemonial banner may then be unsustainable in the long run since not all parties are equally convinced of its benefits. This logic suggests that regionalism can only be used as a strategy to maximize national power by states which are already relatively strong.

Further, as was demonstrated in the discussion on trade policy in 2.4.3, size matters (the optimal tariff argument). Hegemony is not just about market power; it includes systemic power as well. In the event of a large hegemonic power, protection can seem more advantageous because the overall larger market and pool of resources will appear 'sufficient' for the growth ambitions of all members, rooted in the logic of 'import protection in order to export' (Gilpin 2001: 124). We have seen in our exposition of protection that development levels matter; yet it is too simple to say that the one always means the other. For instance, if a region is composed of developing economies dominated by an external hegemon, the region is less likely to be protectionist because the hegemon will almost certainly agitate for some kind of preference (for which, it should be recognized, the hegemon incurs few costs in the form of public goods provision). Member

countries may attempt to counter such external pressure by opting for shallow, relatively poorly institutionalized integration, which lends itself less easily to exploitation by outside powers (as Haggard [1997] argues in the case of ASEAN and the US and Japan). Panic (1995) supports the relationship between depth of integration and political independence, claiming that policies cannot be effective if decisions are imposed from outside. This is not necessarily the case, however: policies can be extremely effective but may not serve the interests of the government in question.

The last factor which will influence the shape and character of regionalism strategies the economic relations which existed prior to the RIA's inception (i.e., on the basis of 'harmonious relations' among countries). Most likely the region will be formed with partners with high degree of preexisting economic relations although, as we have seen in the case of the external hegemon, it is possible that the region be formed among nations whose strongest partners are outside the region. The more intertwined economies are, the more difficult it becomes to pursue national interests. However, interests can be defined more communally by virtue of that interdependence (Panić, 1995), such that international relationships are seen less and less as the main focus of tension. This may be the case, for instance, when economic relations are based on complementarity (Dent, 1997; Cable and Henderson, 1994).

Haggard (1997) suggests that interdependency may act as a substitute for integration, saying there may be less demand (in Asia, for example) for policy coordination *because of* the extensive interdependency in terms of trade and investment. On the other hand, it seems more likely that the less similarity, the narrower the scope of policy areas for cooperation will be, and the shallower (less extensive) cooperation in those areas can be anticipated and the less intensity the RIA will have. Individual actors which are strong but internally divided will be weak. This goes for regions as well. If the member states do not share the same vision and the region becomes a vehicle for political infighting and intra-regional maneuvering, the region will not amount to much. Then there are likely to be other motives driving the integration push, such as 'window dressing', an even greater external threat, or bandwagon effects. At the same time, it is conceivable that a country decides to 'opt out' of regional integration altogether and adopt a 'go-it-alone' strategy.

Regionalism outcomes can be operationalized according to the relative strength and bargaining power of their members, as Van Tulder and Audet (2004) and Ten Napel (1998) have shown (Table 3.3). The typology ranges from egalitarian arrangements, where economic contributions are balanced and where political decisionmaking occurs at the regional level through pluralist voting, to outside-dominated RIAs, where trade and investment are primarily extra-regional and regional institutions are weak or under extensive influence from a non-member state.

The considerations addressed above fit into the logic of strategic feedback loops (section 3.1 and 3.2) because this is nothing else than arguing that previous policy decisions and positioning behavior, and the behavior of others, conditions the strategic reality in the present. The strategic element of regional integration implicitly introduces the factor of time: policy-makers and firm strategists have to deal with a timeline when planning policy and strategy with respect to regional integration. It is important to recognize that this feedback loop runs right through all three levels discussed above. The extent to which the different levels are perceived as harmonious or adversarial determines the relative importance of those levels, and thus the related points in the feedback loop. Regionalism is an attempt to change the power positioning game.

Table 3.3: Regional balances of power

Type	*Regional economic dominance*		*Political dominance in regional institutions*
	Internal trade	*Internal investments*	
Egalitarian	♦ Balanced between all members	♦ Balanced	Voting procedures
Regional oligarchy	♦ Most balanced between oligarchy countries; rest: deficit	♦ Most balanced between oligarchy countries; rest: deficit	Voting procedures
Dual leadership	♦ Balanced between core countries; rest: deficit	♦ Most balanced between core countries; rest deficit	Compromise between interests of core countries
Formal hegemony	♦ Most trade oriented towards core country; rest: deficit ♦ High tech from core/lower tech from rest ♦ *Low* trade within periphery	♦ Investments by core country; rest: deficit ♦ No/low investment within periphery	Dominance by core country
Informal hegemony	♦ Most trade oriented towards core country; rest: deficit ♦ High tech form core/lower tech from rest ♦ *Lower* trade within periphery	♦ Very modest/low investment by core country; rest deficit ♦ No/low investment within periphery	Weak institutions: dominance by core country
Outside dominated	♦ Most trade oriented towards outsiders ♦ Other trade more or less balanced	♦ Highest investments by outsiders; region: deficit ♦ No/low regional investment	Weak institutions: voting procedures or compromises between quasi core countries

Source: Van Tulder and Audet, 2004; Ten Napel, 1998

3.5 Regionalism and the spatial organization of activity

Regionalism outcomes are often discussed in terms of openness, pertaining generally to the degree to which third-party countries can partake in the expected benefits of integration. In section 3.3 it was argued that regionalism is about the spatial organization of economic activity. It was suggested that a fundamental driver of government behavior in organizing economic activity is the desire to increase the value of economic activity within the government's policy space and as well as the value of exports. Location, to the extent it is addressed at all in theory, is primarily considered intra-regionally. However, the arguments presented in the preceding sections, as well as certain segments of the mainstream literature, suggest that regionalism strategies have an *extra*-regional dimension, in the sense that they are a positioning game relative to non-member countries as well.

3.5.1 Understanding regionalism outcomes: inward and outward openness

At the government level, international restructuring is a means of securing power through economic means. Key to bargaining power at the policy level is a government's ability to increase economic activity in the policy space in question, either to reduce dependencies on economic activity in other policy spaces, or to increase the dependencies of other actors on the economic activity within its own policy space. Openness, however, as an element of a strategic game, can have an *extra*-regional dimension, in the sense that regionalism strategies are also a positioning game relative to non-member countries (and non-member, or 'outsider' firms). Thus openness can best be described as having both an *inward* as well as an *outward* character. For instance, governments are benefited by the activities of their 'home' firms in other countries. Not just in terms of taxes which these firms have to pay on foreign profits, but also because this creates some degree of dependency among host

countries, thereby enhancing the home country's bargaining power (Muller and Van Tulder, 2002). Additionally, both dimensions have an internal and an external component (see Figure 3.7). Different combinations of inward and outward openness have varying effects on the spatial organization of economic activity.

Figure 3.7: A framework for positioning regional-level policy preferences

Inward openness		Outward openness	
Inside-in	*Outside-in*	*Inside-out*	*Outside-out*
Openness is a function of reduced restrictions to intra-regional cross-border activity by 'insider' firms	Openness relates to the ability of 'outsider' firms to access regional production networks on a more equal footing with insider firms	Openness relates to the impact of policy as (dis)incentives for insiders to expand or shift into extra-regional production networks	Openness relates to the systemic power inherent in RIA formation and how it affects third parties, other regions and the multilateral system in general

Policy preferences along the two dimensions of inward and outward openness can be expressed both in terms of the national policy space and the regional policy space. Although policy space at the national level remains significant, it would be beyond the scope of this study to go into the international bargaining dynamics that might determine how the preferences of individual countries translate to the collective RIA bargain. It is assumed that member governments must share some specific vision that binds them together, and this study concerns only the expected impact is of that shared vision as expressed at the regional level in terms of the RIA.

Inward openness is defined not only by the ability of regional 'insider' core companies to engage in cross-border (productive) activity ('inside-in'), but also the ability of 'outsider' firms to shift production into the region ('outside-in'), thereby entering the competitive space of insider companies in order to access production factors and intermediate markets to compete on an equal footing. Outward openness has both an 'inside-out' and "outside-out" component. Inside-out openness refers to the presence of (dis)incentives which may exist within the policy space that deter 'insider' firms from seeking growth (or stimulate them to do so) *outside* the region. For instance, governments may take measures against capital flight, tax inordinately the activities of their 'home' firms in third-party (non-regional) countries, or subsidize intra-regional sourcing in an attempt to stem supply and demand 'leakage'. Outside-out openness, on the other hand, is an abstract but very real component to the possible strategic intent of regionalism policies. It refers to the function of a given RIA in the multilateral system, such as its inherent ability to precipitate me-too regionalism strategies ('bandwagon' dynamism) or provide new impetus to the multilateral system (i.e. the WTO's 'third-party' effects considered in Article XXIV of the GATT). In other words, the systemic power which a cohesive region exerts on non-member countries and regional groupings may precipitate more open regimes among the latter in an attempt to counterbalance the spatial effects of the former. The two components of outward openness are at least as crucial as the components of inward openness for shaping the landscape of production and stakeholder relations.

3.5.2 The effects of regionalism policies on openness

As yet these dimensions remain abstract. However, the mechanisms of regionalism explained in Chapter 2 can be used to operationalize the dimensions of inward and outward openness. Since each form of RIA has its own logic and its own combination of policy mechanisms, the mechanisms regulating openness will differ. We therefore return to the mechanisms through which regionalism strategies are pursued (section 2.4) and the institutional outcomes they generate (RIAs) to identify the main strategic component behind each type of RIA. In other words, how do governments intend these policy mechanisms to explicitly shape the spatial organization of economic activity? This question can be addressed by discussing effects of regionalism policies on the locational advantages of the region.

The discussion of economic outcomes of regionalism in the literature (section 2.4.2) deals indirectly with mechanisms of inward openness, but the assumed consequences for location were not yet made explicit. Some measures do not have an explicit locational assumption, however, and many are only relevant in relation to policy measures enacted by non-members and cannot be given a clear value. Here is where the *ceteris paribus* assumption is crucial: if tariffs and investment conditions in the rest of the world remain constant, an increase in the locational attractiveness of a given region should lead to shifting economic activity towards that region. The mechanisms governing inward openness by form of RIA are discussed below (Table 3.4).

For the PTA, openness is governed by the relative reduction in intra-regional tariff barriers and how attractive this makes it to operate within that regional market. This can be a matter of market size, or a regional division of labor. Similar arguments apply to the PCU, except that changes in openness depend on the increase in the CET relative to the pre-RIA situation instead of relative intra-regional tariff reductions. If the CET represents a tariff-barrier increase, it may stimulate extra-regional firms to 'jump' the tariff wall by investing within the region. If the CET represents a reduction, it may signal a reduced incentive to produce within the region. The FTA introduces locational effects of a more serious order in the form of the rules of origin. By requiring goods sold on the regional market to be produced, up to a point, using regional production factors (or risk subjection to tariffs), the FTA is by its nature designed to be inwardly open. Ultimately, *ceteris paribus*, the FTA is designed to attract economic activity through rules-of-origin requirements (a form of rent seeking; Haggard, 1997). The CU is in essence a combination of the PTA and the PCU, with both a relative reduction in intra-regional tariffs and a CET, which allows inside firms to profit from the larger market and lower transaction costs while drawing in outside firms to circumvent the CET. Under the CM, the free movement of factors together with competition policy regulates not only the intra-regional cross-border flows of activity, but the outside-in activity as well. In the EMU, a common monetary policy reduces intra-regional transaction costs, risk and uncertainty. The EPU adds to this a more abstract overall risk reduction, but posits in addition the risk of dealing with a larger government (bargaining partner) when it comes to lobbying.

How these mechanisms regulate outward openness and effect outward dynamics, however, remains underemphasized. Outward openness is difficult to address as it concerns relative (dis)incentives to remain regional or to seek markets, knowledge or assets elsewhere, as well as the responses of other political and economic actors to the RIA. The policy focus is overwhelmingly on inward dynamics, i.e. the changes to the characteristics of the

(regional) policy space and whether core companies respond accordingly with the spatial organization of their activities within that space. Yet it is not only policy-level issues that determine regionalism outcomes; international restructuring concerns the behavior of economic actors and issues of outward openness may be of particular significance to core companies.

Table 3.4: Policy mechanisms and openness

Increasingly extra-regional orientation →

Increasingly deep integration ↓

Form of RIA	*Inward openness*		*Outward openness*	
	Inside-in	*Outside-in*	*Inside-out*	*Outside-out*
PTA Preferential trade agreement	•Intra-regional reductions in tariff and non-tariff barriers to trade and investment	•Intra-regional reductions in tariff and non-tariff barriers to trade and investment	•Intra-regional tariff reductions, changing cost structures, new market dynamics etc. may reduce incentives to seek markets elsewhere	•Intra-regional tariff reductions may induce tariff reductions among non-member states (bandwagon effects)
PCU Partial customs union	•Intra-regional reductions in tariff and non-tariff barriers to trade and investment	•Common external tariff (CET) may draw outside firms into the region	•Depends on locational advantages of the individual member countries	•CET may precipitate 'defensive' strategies among non-member states
FTA Free trade area	•Intra-regional reductions in tariff and non-tariff barriers to trade and investment •TRIMs and rules of origin	•Intra-regional reductions in tariff and non-tariff barriers to trade and investment •TRIMs and rules of origin	•Intra-regional tariff reductions, changing cost structures, new market dynamics etc. may reduce incentives to seek markets elsewhere	•Intra-regional tariff reductions may induce tariff reductions among non-member states (bandwagon effects)
CU Customs union	•Intra-regional reductions in tariff and non-tariff barriers to trade and investment •Common external tariff (CET) to divert extra-regional imports	•Intra-regional reductions in tariff and non-tariff barriers to trade and investment •Common external tariff (CET) to divert extra-regional imports	•Intra-regional tariff reductions, changing cost structures, new market dynamics etc. may reduce incentives to seek markets elsewhere	•Intra-regional tariff reductions may induce bandwagon effects •CET may precipitate 'defensive' strategies among non-member states
CM Common market	•Reduced barriers to trade and investment (free movement of factors) •Should lead to concentration in specific hotspots and a rationalization of business operations	•Market and scale potential in new integrated market •Treatment of investors from member countries versus non-members	•Agglomerating forces deter insiders from seeking markets elsewhere •Competition policy to reduce concentration of market power creates outward pressure	•Intra-regional tariff reductions may induce bandwagon effects •CET may precipitate 'defensive' strategies among non-member states
EMU Economic anc monetary unic	•Reduces intra-regional risk and uncertainty •Facilitates concentration and rationalization	•Regional transparency may attract outside firms by lowering costs of doing business	•Common monetary policy may adversely affect risk-spreading strategies	•May precipitate 'me-too' strategies among other states •May precipitate defensive monetary policies among non-member states
EPU Economic and political union	•Reduces risk and uncertainty •Common monetary policy may adversely affect risk-spreading strategies	•More centralized or harmonized policymaking may attract outsiders by lowering costs of doing business	•Centralized power may reduce insider's ability to play governments against each other	•Enhanced political power may precipitate defensive 'me-too' strategies among other states

In addition to the *ceteris paribus* assumptions with respect to the rest of the world, the logic of international trade and investment policy mechanisms rests largely on assumptions of the relationship between trade and investment. Whether they are substitutes from an economic point of view is a matter of academic debate and the behavior of firms. It should be recognized, however, that they are not substitutes to governments, in that the gains, costs and relevant policy issues differ.

Note also that the vertical and horizontal axes indicate an increasingly extra-regional orientation as integration deepens. Whereas a PTA, for example, primarily addresses issues of intra-regional openness, the EPU carries with it significantly greater political 'weight' and bargaining power. The relationship between depth and outside openness can also be linked to the notion of relative realms of conflict, in that deeper integration signals a higher perception of intra-regional harmony, which by default increases the perception of potentially adversarial extra-regional relationships. Hence sources of conflict are likely to be perceived as increasingly external to the regional members themselves as integration deepens.

In practical terms, changing openness is not only a question of policy-level issues that determine policy-level regionalism strategies. International restructuring is an issue of the restructuring behavior of economic actors, and as argued previously, policy is largely made dependent on assumptions of that behavior, in particular of core companies. To understand the intentions behind regionalism as well as make assumptions of its outcome, we have to return to our partner in international restructuring, the core company. What are the different ways in which governments can perceive firms, and how do governments appear to understand firm behavior based on the assumptions implicit in the policy mechanisms described above?

3.5.3 Assumptions of firm locational behavior

Government perceptions of economic actors' strategic behavior determine the predications upon which economic restructuring processes are founded. Analysis of the relevant literature (Chapter 2), however, reveals that the firm is poorly incorporated into the most theories given their macro-level orientation. Conceptualizations of the firm, as a multifaceted mechanism for the coordination of (international) economic activity, remain highly underdeveloped (Markusen, 2000), and particularly in the case of regional integration (Davies *et al*., 1999; Panić, 1991).

Classical trade theory characterizes national production strategies for a given good as (relatively) intensive in a given production factor. The expected behavior of actual firms can only be derived on the basis of cost drivers (a function of price, efficiency, and demand) which are determined by factor endowments given the universal availability of (exogenous) technology. Yet firms are not explicated; there is in fact no explanation as to the existence of firms at all (as opposed to markets). Cantwell (2000) refers to firms as 'the visible hand' in contrast to 'the invisible hand' of the market, but in effect the 'invisible hand' represents the 'black box' of the firm (Sachwald, 1993), which traditional trade theory does not open. Many of the theoretical assumptions made in academic literature concerning responses to regional integration, the substitutability of trade and investment, and so forth are reflected in the models developed and applied by policy-makers to predict response to policy. Such models are generally macroeconomic and make implicit assumptions about firm behavior and motivations behind strategic decision-making. These

assumptions are often taken as a given, when in fact there is little unanimity as to whether these assumptions accurately reflect behavior, especially at the firm level.

New trade theories and political economy models employ elements like Bhagwati's 'DUPs' (directly unproductive profit-seeking activities) to refer to lobbying and other activities that use real resources to capture economic rents (Feenstra *et al.*, 1996). Although they take an economic view of firms as strategic stakeholders which act and react to their competitors and the environment, and even consider the regionalization of economic activity as an endogenous result of firm behavior, they still have no depth; firms are atomistic. As in international trade theory, these dimensions remain issues of market structure which determine economic behavior, and the firm, if discussed at all, remains an abstraction. Despite the increased recognition of *triggers* of firm behavior, the firm as such is not conceptualized, and is certainly not seen as an actor. At most the firm is considered as an implicit production process, but there remains no place for strategy (Cantwell, 2000) or the firm as an organizational structure (Sachwald, 1993).

Whereas international trade theory considers the international economy as the object of study, with national economies as pieces of the puzzle, other approaches consider the nation-state and the national economy itself as the puzzle and only secondarily address interaction between nations. These approaches (Porter, 1990) reflect an attempt to break open the black box of the national economy beyond factor endowments to identify modes of production and economic stakeholders. Firms are from this perspective carriers of national competitiveness. The 'national business systems' approach (Whitley, 1992) is another variant of this perspective. Yet despite having laid bare the configurations of stakeholders in national business environments and established the key role of firms and policymakers in patterns of economic activity, these theories fail to deal adequately with the issue of regional integration as an outcome of these stakeholder configurations.

Where they fall short is in their relatively static approach to the economic order and the balance between stakeholders in the national economy (cf. Graham, 1997; Hirst and Thompson, 1999). On the one hand, firms are generally typified as e.g. a 'family business' or 'industrial group', and there are no real ideal-types, only organizational outcomes (Sorge in Whitley and Kristensen, 1997). The firm is implicit; a by-product of social actors in their struggle for resources and autonomy (cultural conventions, state structures, financial system; cf. Whitley, 1997). What is in fact considered are differences in the balance between stakeholders in different economic environments. On the other hand, it is striking that RIAs are considered exogenous to national business systems, and in many ways *antagonistic* to the coherence and continued existence of national systems, when it seems more likely that RIAs are endogenous to the dynamic interaction of national systems. In the taxonomies of Strategic Management (e.g. Porter, 1985; Prahalad and Hamel, 1990), firm strategic repertoires essentially represent little more than a continuum of degrees of internationalization. Although Porter-style approaches have been criticized for lack of rigor (consisting of 'frameworks' and not models; cf. Buckley and Casson, 1998) they do, however, introduce the vital distinction between home and host firms.

IPE, on the other hand, considers regional integration as a dynamic restructuring process in which stakeholders bargain for their respective interests. The assumption that home country matters allows for neomercantilist views of the firm as politics by other means (Moran, 1985) or firms as arenas of politics (cf. the 'new diplomacy' of Stopford and Strange, 1991). Firms and governments use their positions to further each other's interests, whether they are shared or not (Vernon, 1971). This line of thinking cumulates with firms

as 'national champions'. Firms are self interested, but manipulable, because they are sensitive to policy-induced uncertainty (Gilpin, 2001) and react to economic triggers in predictable ways (behaviorism). In International Political Economy approaches of this nature, markets in particular are considered abstractions and firms, if conceptualized at all, tend to be lumped together either as manifestations of a capitalist system of accumulation (cf. Wallerstein, 1973) or stakeholders in the 'relations of production' (Cox, 1989).
The theories above can also be analyzed in terms of perceived conflict, using the framework developed by Rugman and Verbeke (1998) in which strategic goals are perceived either as 'conflicting' or 'complementary' (Figure 3.8).

Figure 3.8: 'Goal consistency' between MNEs and governments

MNE-Home \ MNE-Host	Conflict	Complement
Conflict	• Hymer (1976) • Marxist / dependencia theories • Vernon (1971) **1**	• MNE as opportunistic • exit from home • cheap labor seeking • tax evasion • pollution haven seeking **3**
Complement	**2** • Porter (1990) • Strategic trade policy • Political risk literature • Obsolescing bargain	**4** • Vernon (1966) • MNE's as 'arbitragers of interstate growth' • World Bank view; 'Washington Consensus'

Source: Rugman and Verbeke, 1998: 124

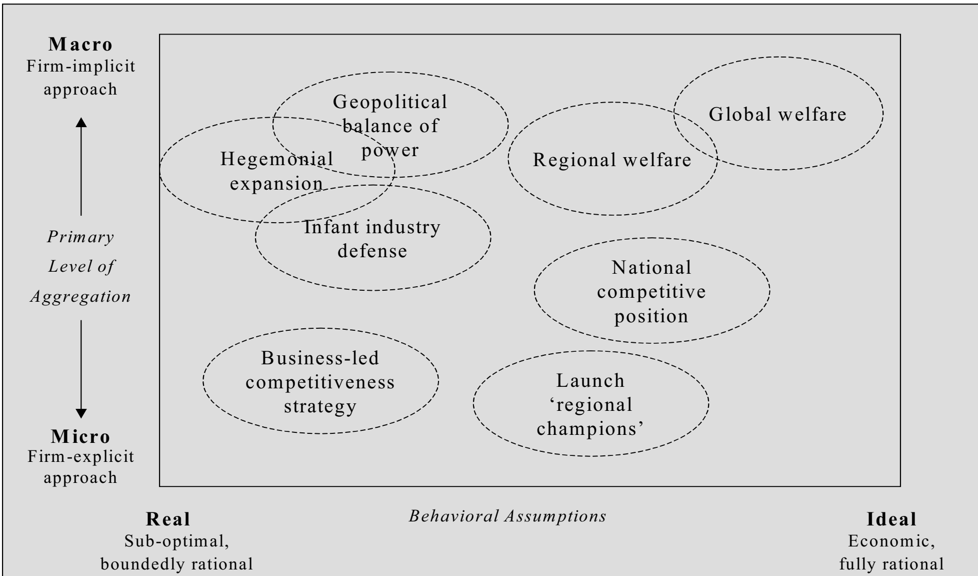
The Rugman-Verbeke framework emphasizes the home and host dimensions of governments and core companies. In quadrant one, MNEs and governments are at odds regardless of home country allegiances. Conflict of this nature is essentially rooted in Marxist analyses of capital accumulation and whether firms are better at it than governments. Quadrant 2 introduces harmonious interests between MNEs and the home country, while the host country regards the MNE with suspicion. Such arguments are based on the assumption that MNE's bring their home country allegiances with them and thus form a threat to a host country's sovereignty. In quadrant 3 the situation is reversed, with complementary goals between the MNE and the host country, while relations with the home country are characterized by discord. In this view the MNE is seen as opportunistic in its attempt to escape home country regulation, and that this behavior may serve the interests of host countries. Quadrant 4 represents the ideology of free markets which is currently in vogue. Based on that ideology, firms and governments of all shapes and sizes

can act in harmony and all accumulate wealth together, regardless of nationality (i.e., the 'alliance capitalism' of Dunning, 1997c).

In the upper right hand corner of Figure 3.8, firms are implicitly inert, responding to behavioral stimuli (policy). Economic change and restructuring is therefore a policy-led exercise. In the lower left, firms are increasingly considered explicitly and, at the same time, as increasingly self-interested and empowered. It seems that the degree of explication is related to the assumption of empowerment (strategically proactive behavior), which in turn is related to the assumption of self-interest. Macro perspectives, possible purely out of necessity, do not reflect a micro-level, firm-explicit understanding. In fact, it seems that the less explicit the approach takes to firms, the more assumptions are likely to be intrinsic.

Essentially the Rugman-Verbeke matrix can be reduced to the idealist-realist dichotomy, considering additionally the degree to which the firm is treated explicitly by the various perspectives. Doing so provides an opportunity to recapitulate some of the main arguments presented thus far by returning to the wide range of policy level rationales for regionalism addressed in the literature, and discussed in Chapter 2 (Figure 3.9).

Figure 3.9: A policy-level repertoire of regionalism



3.6 Preliminary conclusions

It is fair to assume that regionalizing governments think of firms in different ways, depending on the time, the issue in question and which firms are concerned. If relations with home (or host) core firms are adversarial, for example (see section 3.4.2 on perceived levels of conflict), governments may operate on realist terms. If relations are harmonious, firms may be perceived more in idealist terms. If relations are adversarial with other

countries, home firms may be seen in idealist terms at home, but as a realist vehicle for politics by other means in the international arena.

How is firm behavior presented in RIAs, and more importantly, how are arguments presented when policymakers attempt to legitimize an RIA to their citizens, 'outsider' firms and the rest of the world? Given the recent tendency to view the world through a neoliberal lens, RIAs are most likely to be 'sold' to the world primarily in ideal terms. This is not to say that governments do not see firms from a realist point of view, or that they may even enact policies on that basis. As Winters (1999) argues, the rhetoric required to achieve a political outcome does not necessarily reflect the true causes of the endeavor.

Building on the argument of *relative* perceptions of conflict, expectations and assumptions of firm behavior depend on the relative power of the country in question and whether relations with home firms are seen as harmonious. The more market power the country enjoys, the more likely the government is to assume 'idealized' behavior on the part of home core companies. The more harmonious relations with home core companies, the more the government is likely to see relations with host companies as 'adversarial' and thus attribute 'realist' characteristics to their behavior. But, most importantly, they will still enact policies, legitimate their arguments, and make predictions about the response of firms based on assumptions of intrinsic, economic, rational, fully informed behavior. In order to determine whether such predictions are justified, and whether there is tension between the expected behavior of core companies and their real behavior, it is first necessary to explore core companies more closely.

4. CORE COMPANIES AND REGIONALISM STRATEGY

If firms are understood to be key actors in regional integration processes, firm-level theoretical approaches must be investigated to determine what they reveal about firm strategic behavior, the spatial organization of firm activity, and to what extent they deal with the issue of regional integration. The arguments made in Chapter 3 maintain that regionalism-based policy levers are primarily concerned with intra-regional effects, and then largely from an intrinsic perspective.
The current chapter begins by analyzing mainstream theoretical perspectives on the spatial organization of economic activity at the firm level. RIAs concern not only internationalization of policy spaces, but must also be addressed in terms of the internationalization of competitive space, and then with particular attention to the nature of that competitive space. Relevant arguments will be selected based on their 'fit' with the strategic actor approach explored in Chapter 3. Comparing these theoretical foundations with the observations made in Chapter 3 should help shed light on the question of the extent to which policymakers are disposed to 'misperceptions' and failed anticipation of the spatial behavior of core companies, and the consequences this has for welfare, competition and ultimately the welfare and growth goals of the regional policy space.

4.1 Mainstream perspectives on international restructuring

Numerous theories exist which address the firm, firm behavior, and the spatial organization of firm activities, particularly across borders. These theories differ in their assumptions and their level of analysis. As a consequence they can be ordered according to the way in which they conceptualize the firm as a strategic actor, which behavioral assumptions they attribute to actors, and the role of context (strategic reality). Clustering theories according to these criteria generates 5 categories. Firstly, those theories rooted in economic thinking, where the firm is not explicated and the context is generic (classical economics and Transaction Cost Analysis). Secondly, theories which take a more firm-specific view but are acontextual (the Product Life Cycle approach and the 'stages' theory of internationalization). Thirdly, theories that take a view of firms in the explicit context of their environment (Market Power theory, the obsolescing bargain and dependencies). Fourthly, hybrid approaches in which the firm and the context are considered and a wide range of behavioral assumptions apply (management / strategy approaches). Lastly, the OLI paradigm, as an effort to integrate those perspectives, is considered. This will generate a strategic fit with the framework concepts illustrated in sections 3.1 and 3.2.

4.1.1 Market drivers: economics perspectives

The earliest ventures into the significance of location originated with Weber's location theory (1909), based on axioms of classical trade theory and comparative advantage (Dent, 1997). In classical trade theory, production factors are location-specific (such as transport- and labor costs) only later did theory expand to accommodate the externalities flowing from e.g. concentration of industry that allowed for external scale economies. Weber's logic is closely related to the Hecksher-Ohlin factor endowment model, according to which relative factor endowments determine trade. It follows (according to HO) that FDI flows should be greatest between countries with the least similarity in factor endowments.

In classical trade theory, the location of production is essentially a function of factor endowments and all institutional elements are absent. Location is only relevant in imperfect markets (Jovanovic, 2001) because in ideal markets, without transportation costs or cost disadvantages to spreading production, location does not matter. As often as not, firms are a black box and not an organizational structure for production. Classical economic views of economic activity and markets are unsatisfactory from an actor-based perspective, given the proliferation of companies as coordinating mechanisms within the market. Hence the question arose as to why firms exist at all, and whether they are in themselves a market distortion. Coase (1937) addressed the matter by stating that markets and firms were not mutually exclusive because some markets are simply internal to the firm. It follows that firms can *internalize* markets, and will do so if that is more cost-effective. This allowed for the possibility of firms and (more) perfect markets to co-exist because a market would only be internalized if it was less distorted than an external market. Internalization theory looks at the costs of doing business, not just at the cost of inputs (Caves, 1996).

Theorizing cross-border internalization at the firm level introduces the possibility of foreign direct investment (FDI) and intra-firm trade (Bowen *et al.*, 1998). Once the rationale for firms over markets has been established one can consider how firms internalize markets abroad, or why they invest abroad for the purpose of controlling of assets. The answer is largely sought in terms of transaction costs. Transaction cost analysis (TCA) assumes that 'the primary motivation for TNC integration is the belief that a unified control of productive activities in different countries yields benefits to their owner, over and above those that would arise if they were separately owned' (Robson, 1993: 2). Although there are costs inherent to internalization itself, the assumption is that given the inability of markets to allocate resources effectively, the costs of internalization are lower than the transaction costs of using markets to organize activities.

Whereas the major motive for cross-border market internalization in conventional theory has been the reduction of transaction costs associated with tariffs ('tariff-jumping'), more recent work focuses on the exploitation of tangible assets (although former still does apply). This means technology, marketing expertise etc. can best be exploited internally due to their high transaction costs of other modes of doing business (not only licensing, but also trade) (Blomström and Kokko, 1997). Know-how, therefore, appears to be a critical issue in internationalization (Hennart, 2000; Dunning, 1998; Bowen *et al.*, 1998; Caves, 1996). Instead of knowledge being omnipresent and equally accessible to all actors, it becomes an independent variable of its own. On a theoretical basis, therefore, one would expect to see more externalities, spill-over and agglomeration than in the past because know-how has become much more important. This would predict the rise of regional economies (agglomeration) from an economic theory standpoint, as a counter-balance to the politically driven rise of RIAs. These externalities become the 'locational' assets instead of traditional locational assets (production factors) which are inherent to the nation or other form of geographic location.

Buckley and Casson (1976), Williamson (1975) and Caves (1982) further explored the theory of internalization in the international context as a matter of complete contract and incomplete contract theories (Tirole, 1988). Although opinions diverge as to the degree of asset specificity involved in market failure, the shared conclusion is that where cross-border contracts fail, MNEs will arise. Not all contracts can be completely enforceable, however; trust, therefore, plays an important role. The primary difference between Buckley

and Casson (1976) and Williamson (1975) is the issue of asset specificity. The former rely more on the public good nature of intermediate products, such as technology, know-how and more generally knowledge-related 'intangible assets'. In TCA, asset-specificity based approaches still dominate and TNC-related internalization insights are ignored. In the latter, TNCs internalize markets which fail because of intangible assets that exhibit public goods characteristics. As Kay (1991) observed, these need not be specific assets, as TCA would have us believe. IO theory, despite acknowledgement of asset specificity and incomplete contract based perspectives, has still not been open enough to non-specific asset theories.

Kogut and Zander (1993), on the other hand, argue that since much of knowledge is tacit, and therefore difficult and expensive to transfer, it cannot be seen as a public good. Hence their conclusion is that TNCs exist because they are better in transferring tacit knowledge (across borders) than are either markets or other firms. Teece (1977, quoted in Bowen *et al*., 1998) concluded that technology transfers to joint venture partners were on average 5.1 percent more costly than transfers to wholly-owned subsidiaries, while transfers to independent licensees were about 8.7 percent more costly. As Caves (1996) explains, costs are associated with negotiating the terms in advance and haggling afterwards, plus managing the information flow so that the need for the license is maintained over time instead of letting the cat out of the bag. Licensing also entails the risk of brand damage if the licensee does not live up to the standards of the licensing firm.

Logically, larger markets are required to compensate for higher transport costs (Bowen *et al*., 1998). These authors, as do many in mainstream economic research, address the issue of export vs. servicing local markets through investment abroad. Firms' strategic repertoire is restricted to licensing, local production or exports, depending on the exigencies of the business environment. Such studies still assume trade and FDI are substitutes, whereas alternative schools of thought are on the rise that suggest the two are complements. Knowledge as an intra- or inter-firm transferable good or service increases the risk for policy makers of transfer pricing, since it is often difficult to determine arm's length values for knowledge-based, firm-specific assets (Bowen *et al*., 1998).

4.1.2 Responding to environmental change: incremental perspectives

Other theories look at internationalization in stages, i.e. as an incremental process. Key among these are the Product Life Cycle (PLC) theory of Vernon (1966), the internationalization process model of Johanson and Vahlne (1977), internationalization as innovation (Bilkey and Tesar, 1977) and network theory (Johanson & Mattsson, 1988). They conceptualize the firm better, and consider the role of the environment. Markets are no longer implicitly perfect and hence location matters.

Vernon's PLC theory was an attempt to link international trade theory to a firm-level perspective of international investment theory (Melin, 1992) in order to shed light on the sequential development of international production, including the spatial, geographical element. The PLC theory places less emphasis on comparative cost and more on the timing of innovation, scale economies and the roles of ignorance and uncertainty in influencing trade patterns (Vernon, 1966). The focus is a source country of technological development (in his case the US), where the firm bases its initial operations. In the first stage, these products are manufactured locally and exported. In phase two, production commences abroad (Europe) and the US exports to the least developed countries (LDCs). In phase 3

Europe exports to LDCs, displacing US exports. In phase 4 the US has to import from Europe. In phase 5, the LDCs export to USA and Europe. This has a lot of similarity to the world systems theory in political science.

The PLC approach was in fact an effort to integrate the 'neotechnology' approach with Hymer's ownership advantages (see below) (Yamin, 1991). The neotechnology approach emphasized 'not on the specific resource endowment of countries but on the exclusive possession of certain assets by enterprises' (Dunning, 1981: 23). This logic is similar to the internalization theory in that it looks at the role of knowledge in modes and motives of internationalization. As such PLC theory combines an improved conceptualization of the firm with market exigencies to explain cross-border activity. The competition element of the PLC is in its use of technological advantage for a head-start and exploiting those first-mover advantages in international markets.

The stages theory, or Uppsala model, is more of a firm-centric view of internationalization in that the drivers are internal to the firm. Firms internationalize in order to maintain or maximize their long-term profit under changing conditions of the firm in its environment. Inevitably, the only way to do so at a certain point is through cross-border activity. Firm-level internationalization is a step by step process, starting with export and then moving to local production through FDI. Knowledge also plays a prominent role in that export and ultimately the location of production are made based on knowledge of foreign markets. Lack of knowledge is described as 'psychic distance' (Johanson and Vahlne, 1977: 24). Internationalization occurs initially towards countries which are 'psychically less distant', such as immediate neighbors or countries with a shared cultural heritage.

Both approaches assume incomplete knowledge and therefore bear no expectation of fully rational behavior. International activity is implicitly an uncertain and risky endeavor. Yet these inherent knowledge-based disadvantages may not apply to firms with rich experiential knowledge to draw upon. At the same time, incremental models' deterministic character leaves little room for strategizing, with behavior built primarily on costs and economic considerations.

4.1.3 Shaping the environment: power perspectives

Stephen Hymer's (1976) Market Power theory originated in criticism of Hecksher-Olin, due to empirical evidence in the post-war period that showed FDI flows occurred mainly between developed countries with similar endowments. Hymer claimed that a MNE's internationalization strategy had to be viewed within the larger context of its global strategy to increase its market power. According to Hymer, this process 'is rooted in the oligopolistic market conditions within which most MNEs operate'. By exploiting their own unique 'ownership-specific' advantages together with the 'location-specific' advantages of the host economy, MNEs could enhance their competitive position. Kindleberger (1969) adapted Hymer's theory to the monopolistic competition model where production differentiation holds more relevance than oligopolistic interdependence. Caves (1971) also explored this issue and related it to the role of an MNE's ownership advantages. Cowling and Sugden (1987) pursued similar veins of research by analyzing the capacity of multinational market power to generate higher labor surplus induced profit levels. Market power theorists in general emphasize different aspects of structural market failure associated with monopolistic and oligopolistic competition and share some similarities with the NIDL theorists (Yamin, 1991).

Hymer dealt with two separate theories. The most referred to is the firm advantage theory, according to which firms controlled operations in foreign countries because they had an advantage that made it profitable to do so ('firm-specific' advantages (FSAs) or 'ownership advantages'). Differences in location can also be attributed to 'home market' advantages (Hymer, 1976; Knickerbocker, 1973). But the role of the home market is not always black and white, since foreignness can be both an advantage and a disadvantage, depending *inter alia* on home government actions. International production takes the advantage question beyond the industry level, because it concerns advantages in a *particular country* (Hymer, 1976).

His lesser-studied theory is the 'removal of conflict' theory. According to this theory, the more interdependence (horizontal or vertical) exists between oligopolists, the higher the tendency towards collusion, such as market-sharing, price agreements or cartels. If, on the other hand, there are many independent firms and entry barriers are low, there will be less incentive for collusion. It is possible as well that collusion fails and that competition ensues as a result. The more competitive angle was introduced by Knickerbocker (1973) through the concept of oligopolistic reaction, which described the essentially defensive nature of certain internationalization processes.

Ruigrok and van Tulder (1995) draw on similar assumptions of dependencies and a firm's desire to control, but emphasize relations with stakeholders inside and outside an individual firm's value chain as opposed to the relationship between firms. They describe the 'concepts of control' which large, powerful companies exploit to manage the dependent relationships with their stakeholders. The 'obsolescing bargain' (Vernon, 1971) and similar theories (Kobrin, 1987; Encarnation and Wells, 1986), are also concerned with the power-seeking motivations for firm behavior, only in this case with respect to host governments. These studies are important for their exposition of potentially sub-optimal behavior and the chess-like character in their move-countermove aspect (Strange, 1991), as well as the notion that location is relevant beyond simple factor endowments.

4.1.4 Firm-environment interplay: strategic management approaches

Strategy, according to the strategic management (SM) literature, is about the exploitation of competitive advantages. SM is distinct from Industrial Organization approaches in that it tends to be truly micro in orientation instead of meso (Morrison, 1990: 3). According to Morrison (1990), strategy is an issue of matching organizational competencies and abilities with the organization's external context, or 'identifying and exploiting the resources and capabilities of the firm in the marketplace for the purpose of gaining competitive advantage and superior financial performance' (Tallman and Yip, 2001) based on the exploitation of competitive advantage (Porter, 1986; Kogut; 1985). The firm is not considered in isolation, however; elements of strategy include not only setting goals and objectives, but also analyzing industry and competition as well as resources and capabilities. The interplay between firm-internal drivers and external drivers (usually only industry-specific) is summed up in Zou and Cavusgil (1996).

Strategy is also a matter of allocating these resources and capabilities across business activities and geographic space (Hamel and Prahalad, 1998). A key question concerns, therefore, when a location is strategic: as a large source of revenues or profits; as the home market of global customers; as the home market of global competitors, significant market of global competitors; or a major source of industry innovation (Yip, 1992). Therefore in

Strategic Management, competition is primarily about beating out competitors in as many markets as possible. Different patterns of competition are 'strategic intents' that in global industries 'lead to very distinct approaches to competition and the use of competitive advantages, even if the strategic infrastructures appear not to be markedly dissimilar' (Prahalad and Doz, 1987).

Strategy perspectives have inside-out and outside-in variants, which define the drivers of strategic behavior as in or outside the firm, respectively (De Wit and Meyer, 1998), whereby the emphasis is traditionally on the external dimension (Bartlett and Ghoshal, 1989; Porter, 1979). The interplay between both is central to the Strategy literature, for instance in the comparison of comparative advantage (the environment, i.e. location) and competitive advantage (firm-specific, i.e. ownership). The interaction is seen in the way location affects competitive advantage through its influence on productivity and productivity growth (Porter, 1998a).

Internal and external pressures force managers to strike a balance between the economic imperative (internationalization is a response to competitive pressures) which calls for rationalized global operations and the political imperative (the adjustments made necessary by host government demands) which calls for increased local responsiveness (Melin, 1992). As such the issue is not so much why to internationalize (this is a given), but rather how to coordinate the MNE once this has taken place. It leads back to the strategy-structure issue of Chandler (1962). Chandler also took a strategic incremental approach of stages, as did Stopford and Wells (1972).

Yip (1995) identifies four categories of drivers of international activity: the market (Levitt, 1983), cost (Porter, 1986), government policy, (Doz, 1986), or competitive drivers such as cross-country subsidization (Hamel and Prahalad, 1985). All internationalization drivers in strategy are considered relevant in the sense that they have bearing on the firm's ultimate driver, the pursuit of larger markets (Tallman and Yip, forthcoming). The firm's ability to internationalize stems from its competitive advantage, which 'drives both financial performance and the ability to internationalize' (ibid.). Financial performance underlies everything, and relies on growth, market share and profit maximization. To Porter, the strategy of the firm is to strengthen its global position, which it can do by 'transferring strategic assets between different markets which permit it to exploit economies of scale, scope, learning and real options; by the differentiation of products to adapt to national areas and to exploit up-stream competitive advantages and by the flexibility and bargaining strength that a multi-national network provides in managing stakeholders in diverse environments' (Kogut, 1984).

In the strategy literature there is no archetypal global strategy, but numerous ways of competing globally. Hence a set 'strategic repertoire' can be interpreted in different ways, depending on the competitive position of the player in question. Strategy approaches are therefore critical of classical full rationality approaches, on the grounds that strategic problems are difficult to define and do not always have a fixed set of solutions (Rittel, 1972; Mason and Mitroff, 1981; cf. also Caves, 1982). There are not necessarily ultimately optimal positions; rather, each strategic choice and outcome involves trade-offs (Porter 1998b). The strategy literature shares certain perspectives with Hymerian analysis of global competition as a strategic 'game' (cf. the core competencies of Prahalad and Hamel, 1990; Porter's search for strategic differences [1998a] or Porter's 'diamond' as the field of positioning [1980]).

Although much of the strategy literature steers away from economics-style assumptions of full rationality, many of its other assumptions have in fact precipitated many of the recent developments in economic theory, such as scale economies, profit maximization, cost and risk minimization, uncertainty avoidance, the role of competition, the location and exploitation of created assets, and the role of country openness in competition levels. Indicators of this nature are also common in both the theoretical literature and consulting practice on country risk and location advising. The concept of profit maximization or cost minimization, however, does not preclude expensive or 'uneconomical' behavior due to the longer-run perspective in strategy literature. Strategies of preemption, where firms get into markets early even at a cost penalty to corner the market, or dumping as a means to drive weaker competitors out of the market (Doz, 1986) may be an example of a sub-optimal strategy from the perspective of economic 'one-off' models, but in the long term can be rewarding.

The resulting spatial organization of firm activities, described by Porter (1986) as its 'configuration', is usually characterized on the one axis by its global scope (the global / local) and on the other by the level of diversification of the firm. Complementary is the firm's mode of control or coordination, e.g. the multinational, international, global and, finally, 'transnational' organization models of Bartlett and Ghoshal (1989). Firms can see national markets as 'strategic', 'tactical' or 'opportunistic' (Doz, 1986), but ultimately target markets are selected on a cost basis, or on demand (potential revenue) basis. Jovanovic (2001), however, admits that in practice the issue is more complex. Strategic location decisions, for instance, may be influenced by the location decisions of other competing or supplying firms, earlier sunk costs in other locations, the availability of investment funds or demographic effects on factor inputs such as retirement patterns or 'brain drain'. The aim may be low total cost, but locations with low wages often lack e.g. infrastructure, suppliers and mechanisms of maintenance. The effects of low costs are easy to measure up front, but productivity costs remain hidden or unanticipated (Porter, 1998a). Ultimately locational choices should weigh overall productivity potential, not just input costs or taxes.

The strategy literature has been criticized largely due to the wealth of variables, strategies, factors it supplies. Its breadth is in many ways seen as its weakness, generating 'frameworks' instead of theory (Casson). In fact its practical orientation leads to a higher emphasis on managerial relevance than on theoretical elegance (Melin, 1992). The 2x2 frameworks for which it is famous have served strategic management well, but they are 'far from ideal' (Morrison, 1990: 142). Furthermore, the concept of internationalization lacks refinement in that it tends to throw all non-domestic solutions onto one big pile. As problems with dichotomizing international competition are mounting, the global-local continuum is no longer adequate. Bartlett and Ghoshal admit their transnational strategy model is a hypothetical solution that 'does not correspond to any one company' (Morrison, 1990: 143).

4.1.5 The OLI paradigm

While Hymer and Vernon launched FDI as a field of study in its own right and introduced the concepts of ownership advantages and location advantages to the literature, Dunning (1977) combined the two with the internalization perspective (TCA) in his 'eclectic' OLI paradigm as an all-encompassing 'framework' for FDI (Cantwell, 2000). In the words of

Dunning, 'the theory of foreign-owned production stands at the crossroads between a macroeconomic theory of trade and a microeconomic theory of the firm' (Dunning, 1998: 19). OLI was in fact aimed primarily at making internalization theory more dynamic (Melin, 1992) by endogenizing some of the 'environmental' issues that firm theories neglect.

Ownership (i.e., firm-specific) advantages form the basis for the firm-level strategic repertoire and can be seen simply as unit-cost reducing relative to competitors (Dunning), or as a means to suppress competition by raising barriers to entry (Hymer), or as a weapon which sustains competition between rivals (see 4.3). Internationalization depends on a combination of location and governance decisions (Dunning, 1977; Dunning, 1981). Of the three types of advantage, the least attention has been paid in the International Business literature to location. Dunning (1998) emphasizes the renewed attention for the spatial aspects of investment and production instead of the emphasis on firm-specific determinants, returning to the questions set by new research agendas which seek to pay more attention to the spatial aspects of value-added activity.

OLI, just as internalization theory, is primarily rooted in economics, with transaction costs and factor costs as main explanatory variables and assumes rational decision-making in firms undertaking FDI (Melin, 1992). OLI does not have a fixed view of competition nor a theory of the firm, and its structure-conduct-performance approach is too static (Cantwell, 2000). OLI is not a theory of the firm, but one of firms and / or countries (Dunning, 2000). By linking so heavily to internalization theory, it overemphasizes the national dimension. The focus remains on 'the advantages that one firm has over another that allows it to compete in that other firm's home country' (cf. Dunning, 2000), where 'home country' is better replaced by the term 'competitive space'. International dimension of firm behavior, firm strategy with respect to spatial organization of activity, but regional integration is either ignored or seen as an extension of existing theory (change to locational advantages, possible harmonization of ownership advantages etc.). Efficiency, from the firm strategy point of view, is not always optimal (Cantwell, 2000).

4.1.6 Evaluating theory from a strategic actor perspective

In TCA the question is an economic calculation of markets versus hierarchies. Strategic management literature focuses on firm strategic reality in terms of cost minimization and profit maximization, growth, and risk mitigation, often at the industry level. Strategy is often left out of International Business literature, which considers markets and industries, as well as the organization and structuring of the MNE itself (Tallman and Yip, forthcoming), and as such tends to overemphasize the 'sunny side' of firm behavior (Eden and Lenway, 2001). As Table 4.1 illustrates, there is a focus on intrinsic considerations in much of the theory. Only Hymer's Market Power hypothesis hinges on intrinsic and extrinsic considerations. The contrast between intrinsic and extrinsic considerations is reflected in the debate between 'structural' and 'transactional' market imperfections. Hymer has been widely criticized for focusing on 'structural' imperfections instead of 'transactional' ones (Dunning and Rugman, 1985) although Hymer did, in fact, address 'internalization' in his thesis (Hymer, 1976: 48).

Table 4.1: Theories of the firm, strategy and international restructuring

	Main authors	*Conceptualization of the firm*	*Conceptualization of competitive space*	*Drivers of behavior*	*Strategic focus*	*Level of analysis*
Internalization theory	Coase, 1937; Buckley and Casson, 1976; Hennart etc.	Bounded rationality, opportunism?	Absent	Costs of doing business (transaction costs)	Optimizing transactions, cost minimization	Micro
Product Life Cycle theory	Vernon, 1966	Incompletely informed; led by deterministic, predictable behavior	Competitive oligopoly	Technological advantage	Exploitation of technological advantage	Micro / meso
Stages theory of MNE	Johanson and Vahlne, 1977	Incompletely informed; led by deterministic, predictable behavior	Market opportunities characterized by 'psychic distance'	Growth and long-term profitability	Acquisition of knowledge	Micro
Competitive advantage	Porter, Yip, Bartlett and Ghoshal	Strategic actor vying for edge in competitive 'game' with incomplete information	Source comparative advantage and location-based assets	Profit maximization through scale, risk minimization, competitiveness	Competition: survival of the fittest	Meso
Market power	Bain, 1956; Hymer, 1976; Cowling and Sugden, 1987	Rational decision-maker	Collusive or competitive international oligopolies / monopolies	Profit maximization through control and collusion	Anticompetitive : Collusion, raising entry barriers	Meso
Bargaining power	Vernon, 1971; Kobrin, 1987; Stopford and Strange, 1991; Ruigrok and Van Tulder, 1995	Strategic decision-maker Boundedly rational but self-interested	A complex web of positioning possibilities and push and pull forces among bargaining relations	Profit maximization; rent-seeking	Maintaining control over value chains, bargaining processes, resources and technology	Micro / meso / macro
OLI paradigm	Dunning, 1977; 1982; 1993	Rational decision-maker	A selection of cost calculations	Costs of doing business (transaction costs)	Matching OLI advantages	Macro / micro

Yamin's (1991) criticism of TCA is aimed at its tendency towards self-fulfilling prophecies. To sustain the argument that efficiency is the focus of firm strategies, it is *necessary* to assume that transaction costs occur naturally and external to the firm. In the eyes of many researchers (Hennart, 2000; Yamin, 2000), the debate has subsided under recognition that the two are not mutually exclusive explanations. Although TCA is focused on efficiency (intrinsic motives) for cross-border activity, it can actually provide added justification for Hymer's view that monopoly and market power give rise to MNE, if e.g. conflict resolution and transaction costs complement each other in that market power is only possible under certain cost conditions, like switching, searching, and sunk investment. Hennart (2000) defends the attempt to link TCA to a wider range of phenomena by arguing that TCA is more of an 'approach' than a theory. Dunning (2000) questions this strategy of defining market imperfections ever more loosely (e.g. Rugman's view), arguing that it sabotages the incisiveness of the transaction cost view, since a theory that explains everything, explains nothing.

On the other hand, a number of theories emphasize risk and uncertainty as key drivers (Knickerbocker, 1973; Cyert and March, 1963; SM). According to Knickerbocker (1973), there are two determinants of firm conduct which underlie the choice of competitive

strategy: uncertainty avoidance and risk minimization (the two are not necessarily identical). Risk is often thought of in political terms, but risk can also be reduced within the value chain, through e.g. downsizing, outsourcing, the exploitation of core competencies, or the development of flexible networks (e.g. Rugman, D'Cruz, Verbeke). Spreading production across geographic space can also be seen as a risk-mitigating or risk spreading strategy (Rugman, 1976). Hence, for Yip (2001) the choice is not 'why internationalize', but rather 'why not'?

The second dimension of critique relates to the attention given to competition and competitive positioning. Competition has been seen as largely static and as resting on cost minimization in relatively closed economies (Porter, 1998a). Initially the basis was comparative advantage, more recently economies of scale. According to Porter, competition must be seen as dynamic, as the search for strategic differences. The role of location in the search for strategic differences has been misleading because thinking on location in recent decades has taken a relatively simple view of how companies compete (Porter, 1998a). Location affects competitive advantage through its influence on productivity and productivity growth.

In other analyses, competition is absent altogether, such as TCA and the incremental approaches. The need to incorporate oligopolistic interaction issues has been recognized (Cantwell, 2000). Buckley (1990) and Buckley and Casson (1998a) have both acknowledged the need to incorporate advantage and oligopolistic interaction-based issues in their analyses, although in their understanding cooperation is no more than an issue of efficiency (Yamin, 1991). TCA is therefore more an analysis of the *firm* than of firms (Cantwell, 2000) and its understanding of the MNE is static (Melin, 1992). A theory of firm behavior, however, depends not only on what kind of firm is being considered, but also what kind of structural or institutional environment the firm operates in: 'the key to understanding fruitfully the characteristics of a firm's activities is to conceptualize its environment' (Sugden, 1991: 171). Additionally, the argument that TNC has emerged to minimize transaction costs does not on its face prove it is efficient (Cowling and Sugden, 1987: 10). Hymer made similar observations, in that his focus was on profit maximization, but that he astutely observed that an advantage (FSA) may make control desirable for other reasons than direct or short-term profit.

The final point of critique concerns the nature of core company relationships with other strategic actors, such as governments, suppliers, customers, trade unions. Much of the literature ignores these relationships, and the bargaining literature is almost exclusively aimed at interaction with governments alone. Hymer himself considered only power relationships with respect to other companies. Although Porter's diamond addresses competition, value chain partners and governments, it unfortunately provides only a static analysis and confuses 'factors' with 'actors' (Ruigrok and Van Tulder, 1995). Understanding the strategic behavior of core companies requires a vision of relationships with actors of multiple types.

4.2 Core companies and bargaining relations

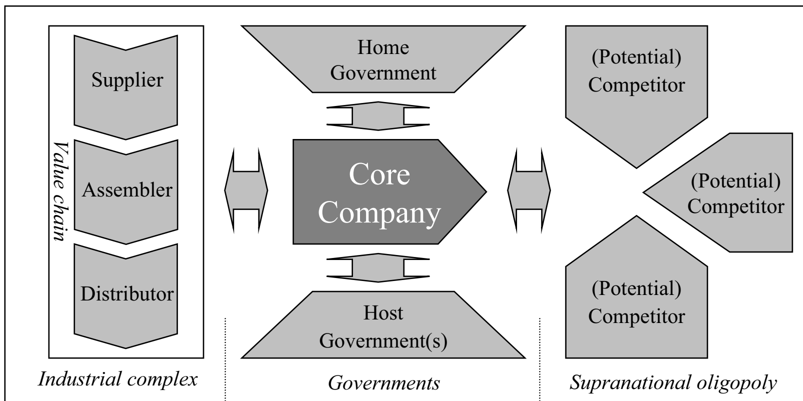
The theories above contribute much to our understanding, but they hinge on a wide range of divergent assumptions and emphasize different aspects of behavior. They exhibit shortcomings for the purposes of this study on the basis of several key ingredients of strategic actor approach applied here. Firstly, on the basis of their behavioral assumptions

(emphasis on intrinsically-driven behavior); secondly, their perspective on positioning behavior (tendency to see the firm in isolation or to misunderstand the nature of competition); and thirdly, the way context is addressed (a tendency to downplay the role of bargaining relations with key stakeholders in the strategy process).

4.2.1 Strategy preferences and perceptions of conflict

In considering the identification of strategic options and the choices made, strategic reality and strategic intent at the core company level can be defined along lines similar to those used for policymaking in Chapter 3. In a world of bargaining, power and positioning, strategic choices are made on the basis of perceptions of conflict. For core companies, three different realms of potential relative conflict can be discerned: at the level of the 'industrial complex' (Ruigrok and Van Tulder, 1995), in the form of relations between the core company and suppliers, customers and trade unions; at the government level, in the form of relations with home and host governments; and at the level of supranational oligopoly, in the form of relations with other core companies (Figure 4.1).

Figure 4.1: Managing relations in core spaces



This constellation of strategic interaction characterizes core companies' competitive spaces. Table 4.2 explores the three levels of stakeholder interaction and describes in broad terms a core company's strategic orientation based on perceptions of harmonious or adversarial relations at each level (once again it must be stressed that perceived harmony is only relative).

At the level of a core company's individual industrial complex, perceptions of the level of conflict in its relationships will either generate strategic efforts aimed at preserving the cohesion of the 'nexus of stakeholders', or at altering that balance of power through e.g. pressuring trade unions, squeezing suppliers or choking market channels. At the government level, harmonious relations are characterized by fostering a perception of symbiosis, or a win-win situation akin to what Dunning (1997b) calls 'Alliance Capitalism', while strategy under conflict centers on pressuring policy space(s) through e.g. the exercise of systemic power or the threat of exit. Finally, the nature of relationships

with other core companies, characterized here as a supranational oligopoly, can lead either to competition (in the Porterian sense) or collusion (in the Hymerian sense). The supranational oligopolistic character of relations between core companies will be discussed in more detail below.

Table 4.2: Realms of perceived conflict in competitive space

Level	*Focus of strategy*	*Perceived relationship*	
		Harmonious	*Adversarial*
Supranational oligopolies	Other core companies in supranational competitive spaces beyond the scope of policy space	Collusive behavior, e.g. price agreements, cartel formation, non-penetration of other core company complexes	Competitive behavior, e.g. dumping, preemptive investment, raising entry barriers through value chain capture
Governments	Governments, both home and host.	Symbiotic win-win situation; shared strategic reality in policy and competitive space	Eliciting incentives through lobby behavior, threat of exit, systemic power etc. with minimal concessions
Industrial complex	Stakeholders within the industrial complex, in particular value chain partners (suppliers and customers) and trade unions	Preservation of stakeholder consensus	Pressuring trade unions, suppliers, and customers, choking market channels through broad horiz. positioning etc.

Core companies, by their very nature, are predisposed to anti-competitive behavior as part of their effort to reduce conflict. In their drive to preserve their positions at the core of their respective complexes, core companies are very extrinsically oriented. These extrinsic strategies relate in particular to three categories of bargaining partner: governments, (value chain) partners within the core complex, and other core companies. Firms adapt their positioning, act to preserve core status and try to shape their competitive and institutional environment.

Core companies want to preserve their core positions in the long term. Strategy preferences (choices from a strategic repertoire) are focused on perceived areas of conflict, and geared towards removal of that conflict (Hymer's reduction of conflict thesis; see also Porter and Fuller [1986] on the importance of 'conflict resolution'). Conflict removal with respect to other core companies comes down to the question of collusion versus competition. Core companies only view other core companies as competitors to a limited degree. Hymer's (1976) conflict-reduction thesis, however, was aimed only at oligopolistic behavior of economic actors, whereas the context of the strategic actor approach begs for analysis of conflict with other types of actors.

The reduction of conflict extends beyond relationships between core companies. Bargaining is an issue of rent sharing, and strategies for rent-sharing depend on positioning relative not only to other core companies, but also to governments and to other stakeholders. Conflict removal with respect to governments and value chain partners has to do with bargaining power and managing dependencies. Since bargaining power is related to dependency (Ruigrok and Van Tulder, 1995; Kobrin, 1987), a strategy built around power and influence must consider the degree to which the actor is dependent on the choices and actions of other actors, and vice versa.

These ideas are counter to strategic management theories which blend intrinsic and extrinsic motivations, also because positioning is less about developing distinctive competencies than about developing distinctive, independent industrial complexes.

Transaction cost analysis is also inadequate due to its overwhelmingly intrinsic orientation and lack of contextual perspective. Strategies are not solely driven by exogenous economic triggers because core companies have enough power to influence market conditions (distorting the market instead of responding to the market), particularly when it comes to their own competitive spaces. Core companies generate ('structural') market distortions through their market and non-market strategies; they are not an economic answer to ('natural') market distortions.

Firms can apply both non-market and market strategies in positioning, bargaining and managing dependencies. Non-market techniques generally refer to lobby activity, whereas market techniques imply marketing, production and organization behavior. Market strategies imply the introduction of market distortions of different kinds (the perfect market does not exist and never has), both intrinsically and extrinsically motivated. They may consist of the generic strategies of Porter (cost leadership, cost focus, differentiation and focused differentiation); market seeking, asset seeking, or sourcing strategies, but also entail the use of economic muscle to sway policy outcomes, such as transfer pricing or the threat of relocation. Often the two techniques are used in combination (e.g., the threat of relocation is the leverage behind the lobby). The emphasis in the literature is on market-oriented strategy because competitive space is assumed to be more important than policy space for firm strategies. Both market and non-market strategies can be what Bhagwati calls 'directly unproductive' activities (DUPs), where the emphasis is on shaping the environment to one's bargaining advantage instead of production *pur sang*.

In keeping to the framework devised in Chapter 3, the strategic behavior exhibited with respect to conflict reduction and the management of dependencies can be analyzed in spatial terms. Strategic responses, spatially, involve influencing bargaining and competitive relationships through location decisions and the organization of activities. Jovanovic's (2001) assumption is that firms want to maximize profit and minimize operating costs and any 'penalty' associated with different locations. That penalty, however, is generally quite limited for core companies, as they generally have sufficient market power to distort the market in other ways which 'compensate' for that penalty. This reiterates the assumption that core companies, as strategic actors, are not restrained by 'exogenous' circumstances beyond their control. Furthermore, understanding strategy as an issue of power relations among individual actors has a realist bent. As soon as actors are defined, their interests become more and more realist and less idealist, since idealism is associated with abstractions. Once an actor has a face and a name, it becomes self-interested.

4.2.2 Core companies and oligopolistic competition

There are a few reasons to justify the emphasis on core companies in regionalism. Jovanovic (2001) argues that, generally, most restructuring will take place over a longer period, in large part because information takes time to get around and companies do not always know what is 'expected' of them. Core companies, however, are not subject to information asymmetries of this nature because they are part of the preceding political process and therefore able to respond immediately, or even proactively. Furthermore, they lead the restructuring process, particularly in its international dimension: according to UNCTAD (1998), fifty US firms account for 60% of the entire US outward FDI stock.

It is useful to see the micro-reality of location, particularly in the cross-border context, as related to the nature of market structures and competition (i.e.; polypolistic, monopolistic, oligopolistic). Most Industrial Organization (IO) perspectives consider the decision to undertake cross-border productive activity as a logical outcome of an oligopolistic environment (Knickerbocker, 1973). As a consequence, oligopoly is a key ingredient which in effect makes Industrial Organization approaches meso more than micro. From an 'internalization' perspective, the firm is not really competing, only selecting from environmentally conditioned options and as such a passive reactor to environmental change (moreover, internalization is an issue of intermediate markets, not product markets). Oligopolistic competition implies multiple producers for a given market, which in economic terms remains (artificially) defined by product categories (in reality the line between 'products categories' and thus 'industries' is quite arbitrary).

Oligopoly means the field of players is manageable and limited. Therefore positioning strategies are not only necessary but also feasible. In a game of positioning, an actor has a range of options ('strategic repertoire') to choose from, not all of which are equally viable for every firm (cf. Caves, 1996). Oligopolistic firms can and do choose a course of action that anticipates the behavior of their competitors, a dynamic which economists are unable to model reliably (Gilpin, 2001). Thus the strategic behavior which emerges from oligopolistic structures means that actions are determined by drivers other than static circumstantial factors.

Core companies' overriding strategic operative, the preservation of their core position, can be expressed in terms of market power (cf. Robson, 1993). Lall (1976) defines market power as 'the ability of particular firms, acting singly or in collusion, to dominate their respective markets (and so earn higher profits), to be more secure, or even to be less efficient than in a situation with more effective competition…the concept may, of course, be applied to buyers (monopsonists) as well as sellers' (quoted in Cantwell, 2000: 14). Market power implies being a price maker instead of a price taker. Encarnation and Wells 1986: 'competition among governments in the market for foreign investment is analogous to competition among producers for market share.' Core companies are themselves an agglomeration of power in a field of limited power (oligopoly). This can also relate to policy space, and therefore also to RIAs.

Ultimately, the oligopolistic nature of firm interaction poses two overarching strategic options: rivalry or collusion (similar to competition and collaboration in the 'embedded firm' perspective; De Wit and Meyer, 1998). Hymer and Rowthorn (1970) were the first to truly consider oligopoly in the international context. In Hymer's Market Power theory, firms collude in anti-competitive behavior to prevent new entrants. Oligopoly already suggests that optimal positioning in the economic sense may not be necessary and opens the possibility for sub-optimal behavior. This is simply because a firm's rent-generating capacity may not be seriously threatened by its competitors (Doz, 1986). Moreover, this absence of threat may be an implicit or explicit 'gentleman's agreement' by which core companies choose not to threaten each other's rent-generating capacity (what Scherer [1980] calls 'exercising mutual restraint').

If there were real competition among core companies, there would be a price war with negative consequences for all. Avoiding such situations therefore becomes the 'first concern of corporate policy' (Baran and Sweezy, 1966: p. 57). Thus collusion derives in part from recognition of the retaliatory power of rivals (Cowling and Sugden, 1987: 17). Price wars are particularly damaging for (innovative) products at the front end of the

product life cycle, from which core companies gain the bulk of their advantages. Core companies owe much of their core position to their control over and exploitation of core technologies (Van Tulder and Junne, 1989). Positioning based on innovation secures a longer term core position. The temporal aspect is vital as 'being a key player is not a state, but a process' (Jovanovic, 2001: 32). Hymer also emphasizes the long term ('the large firms of the world are all competing for these various sources of future growth…') but securing a stable core environment leads in his view to competition in 'an oligopolistic rather than in a cutthroat way' (Hymer, 1979: 82). These large internationally active oligopolists 'recognize their mutual interdependence and strive to share in the pie without destroying it. As they do so they come to be less and less dependent on their home country's economy for their profits and more and more dependent on the world economy. Conflicts between firms on the basis of nationality are thereby transformed into international oligopolistic market sharing and collusion' (Hymer, 1979: 82).

In fact, it can be argued that core companies are actually quasi monopolists. They try to keep differentiating themselves from others, repositioning to maintain their own identity. Consequently, identifying competitive spaces is difficult; markets can be thought of in product categories (SIC codes etc.) but core companies cannot. Although their positions change, their existence is much more stable: they generally do not wipe each other of the competitive map. Competition works best when firms think they are working towards a monopoly position (at best) and an oligopoly (at worst) (Jovanovic, 2001). If core companies know that oligopoly is the setting, why should they bother to compete fully? In other words, core companies collude because they wish to avoid the perfect competition which would otherwise erode their profits (Cowling and Sugden, 1987).

Core company spatial organization strategies and corresponding locational decisions must be seen in the context of a core company's positioning between collusion and competition (Cowling and Sugden, 1987) and their 'signaling' strategies with respect to one another (cf. Slager, 2004). According to Yamin (1991), lack of integration in world economy was generally seen as the basis of costs and disadvantages of foreign operations. As the world economy integrates, monopolistic advantages may no longer be necessary to offset costs. Barriers to internalization would fall, but this would lead to even greater cutthroat competition, which core companies want to avoid. Plus the costs of internationalization for companies which are already international are considerably less than the costs of initial internationalization, which TCA and Hymer were both considering. In fact, as firms become increasingly international and exposed to more bargaining partners, the handling of conflict becomes of greater importance. Internationalization and geographic spread function as a risk mitigation strategy, whereby the risk is of losing one's core position, and conflict resolution is the means to make the spread strategy feasible. For core companies, transactional uncertainties are considerably less significant than the conflict uncertainties.

4.2.3 Core company interaction with governments

Hymer (1976) and Vernon (1971) were among the first to direct attention towards firms as economic actors with political impact. Core company strategy in institution-building comprises techniques of influencing the regulatory environment. Generally the regulatory regime is seen by business actors as a 'thicket of rules' (Braithwaite and Drahos, 2000: 18). As such governments have often been seen as an obstacle to international strategies, although some now see them as a source of opportunity (Gilpin, 2001; Krugman, 1991;

Porter, 1986). To many, the function of government as far as firms are concerned does not extend beyond the provision of economic and technical uncertainty, interest rates and fiscal conditions (Doz, 1986). From a firm point of view, policymakers are here to guarantee macroeconomic stability, efficiency of inputs and infrastructure, and to establish the rules of the game (Porter, clusters 1998). Milton Friedman (1962) notes four functions that government performs for business: to serve as a rule maker and rule enforcer; to provide a common monetary authority; to control the negative consequences of monopoly power; and to take care of those who cannot legitimately participate in the system (for example 'madmen' and children) (cited in Wartick and Wood, 1998: 43). Dunning, on the other hand, sees only two legitimate interventions for governments: protection of infant industry, and countering anti-competitive behavior (Dunning, 1997b).

Assumptions of the role of government are a part of core company strategic reality. The relevance of policy, however, has been understated in much of the literature. Doz (1986) argues that an analysis of government policies should be an integral part of strategy making. 'A middle level analysis is required to understand these policies and try to anticipate them. Merely studying their explicit manifestations – codes, laws, regulations and the like – would ignore the opportunity to anticipate and even influence them by studying their dynamics and understanding the concerns, motives and logic of government intervention' (Doz, 1986: 258). Yet the assumptions of government behavior illustrated above are highly idealistic, dramatically understating the possibility of strategic behavior on the part of governments. It is possible that firms are more likely to have a realist view of policymakers than the other way around. The strategic use of public policy has been dealt with extensively in the literature; firms establishing a presence in Europe pre-1992, for example, were able to influence policy outcomes to suit their interests (Wartick and Wood, 1998). Rugman and Verbeke (1994) also convincingly argue that firms pursue 'shelter' strategies aimed at imposing artificial costs on rivals without positively affecting own core competencies. This implies the pursuit of *extrinsic* strategies (lobbying for protection) to avoid the necessity of *intrinsic* strategies (increased competitiveness) as strategic behavior on the part of firms (see also section 2.5). Rugman and Verbeke's arguments also imply that firms don't always share their strategic reality with governments when trying to realize shelters through political activity, since the use of protectionism (strategic trade policy) is usually legitimized by allegations of potential for superior profits or technology spillover, which are often untrue.

Incidentally, this also suggests that non-market strategies have spatial dimensions, since a firm's lobbying impact is greater if the firm is actually present as an economic actor within the institutional sphere it tries to shape (Baron, 2000). Similarly, 'market players who stand to gain the most from integration will be the most active in lobbying for it' (Mattli, 1999a: 3). Firms can influence policy as well simply through new ways of doing business, such as just-in-time production (JIT) which change *de facto* the business environment. Generally this in turn forces a policy response (actor interaction). Massive capital flight, for instance, can lead to a new institutional setting for capital controls. Another example is a shift towards increased vertical integration across geographic space and the resulting global division of labor. This is in itself a new way of doing business which can prompt policy interventions that formalize (institutionalize) the new rules of the game.

Studies by Lipson (1985), Bennet and Sharpe (1985), Evans (1979) and Moran (1974) suggest that the attractiveness of an investment site often depends on the relative bargaining power of the investing firm and the host country state and / or the degree of

political risk associated with the host country (see also Moran, 1985). According to Gatz (1997), multinational enterprises see instability as the principal deterrent to investing and operating abroad. Despite its insights, the political risk literature assumes the decision to internationalize has already been taken (or is inevitable); the question remains *what motivates the original decision*, not what the go/no-go criteria are.

The relationship between policy strategy and core company spatial organization strategies relate to bargaining power. Certain strands of International Organization have fused with elements of political economy to take firm-government interaction better into account while attempting to carry the discussion farther than 'firms as profit maximizers and governments as policy realists' (Vernon, 1994). Graham (2000) introduces game theoretic perspectives to firm behavior in order to develop inter-firm rivalry better, while Muller and Van Tulder (2002) explore the strategic intent of policymaking in relation to firms and their internationalization strategies. Dunning (1986) lists six dimensions of activity by internationally operating firms with potentially negative consequences (supply and / or demand leakage) for a country's growth regime: the transfer of resources, the control of resources, sourcing strategies, domestic competition effects, the distribution of value-added, and the impact on the international allocation of resources. Geographic spread can enhance bargaining power, but concentration can as well, if only relative to different partners.

In much of the literature, the emphasis for both firms and governments is placed on competitiveness. Unfortunately discussions of competitiveness can in themselves become a level of analysis problem because it is not always clear what competitive means. On the one hand there is macro-competitiveness, emphasizing e.g. the balance of trade and price developments (cf. Sachwald, 1993); on the other hand meso-competitiveness, where market variables such as factor and demand conditions are key (cf. Porter); and additionally micro-competitiveness, which emphasizes the ability of individual firms to be successful in their respective markets. Some analyses have reversed the question, saying that firm level competitiveness is a function of national competitiveness (like Whitley etc.), but this overemphasizes the role of the home diamond in firm strategy. Core companies are precisely core companies because they are largely the cause of the diamond and not simply shaped by it, and core company strategies are defined at the level of the firm, not sector (Rugman and Verbeke,1991).

Maintaining core position is key in general and regional integration is part and parcel of a strategy in this regard. One element of strategy in maintaining core position relative to governments is that of geographic spread. Spreading is a risk reduction strategy (Rugman, 1976) by which firms can counterbalance new pressures from governments (Phelps, 1997; Muller and Van Tulder, 2002). Moreover, core companies are generally able (financially, in particular) to manage the risks inherent in spread, which tend to be lower than the risk of 'policy capture'.

4.2.4 Core companies and bargaining within the industrial complex

Core company international strategies also have to do with perceptions of conflict among stakeholders within core industrial complexes, particularly within the value chain. Relations at this level hinge largely on the dependencies and interdependencies of various actors. In this way their bargaining power is defined. Strategies to this end relate to the

management of the various dependencies within a core company's industrial complex (for a more detailed exposition see Ruigrok and Van Tulder, 1995).

Relationships can vary from complete independence to one of total dependence, where the value chain partner has no influence on core strategy and production decisions. The 'concept of control' of the core company varies accordingly from one of cooperation / competition to one of structural control, respectively. Different degrees of dependency are suited to different types of network configurations. Whereas independent partners will engage the core company in an egalitarian network, a relationship of complete dependence will translate into structural control. This scale of dependencies in fact parallels the debate on post-Fordism (see section 3.3) as the egalitarian network represents the flexible specialization paradigm of Piore and Sabel (1984), formal control networks represent the Fordist production paradigm, and structural, informal control describes the Toyotist relationship between core company and value chain partners.

In their global positioning strategies, core companies look increasingly for long-term planning relationships with members of the industrial complex. Whereas in the past core companies had multiple-sourcing agreements which served to play suppliers against one another, the trend is currently towards single-sourcing agreements, whereby relationships are more exclusive (Ruigrok and Van Tulder, 1995). This reduced interpenetration of core complexes is a parallel to the collusive core company gentleman's agreement.

One of the means through which core companies can attempt to gain competitive advantage is by squeezing value chain partners. Both collusion and competition, however, can have detrimental effects for core company network partners. Collusion may be detrimental because it makes it difficult, if not impossible, for partners to play core companies off against each other, and competition may be detrimental because the higher bargaining power of core companies in general means that the costs of competition are more likely to be borne by other members of the industrial complex.

Peoples and Sugden (2000) also explore collusion between firms, but then in terms of setting wages. Here internationalization becomes a means to sabotage labor's ability to organize on a company-wide basis (Cowling and Sugden, 1987). The collusive, intra-regional gentleman's agreement hinges on the assumption that inputs, be they labor, intermediate goods or raw materials, are finite and to a certain extent location-bound. Collusion is unnecessary if there are infinite resources, but in the real world collusion takes place with respect to inputs to avoid 'race to the bottom' strategies based on competitive cost alone. Peoples and Sugden (2000) describe this as the 'divide and rule' tactics of MNEs with respect to labor.

Under increased potential for conflict, internationalization strategies may alleviate tensions. Companies have been shown to *withdraw* from their home countries to exert pressure on other domestic stakeholders, be they governments or value chain partners (Vernon, 1998; Ruigrok and Van Tulder, 1995). Thus by *dispersing* activities (increased cross-border production), as opposed to consolidation of production in a single country within the region, core companies can enhance their bargaining power relative to regional value chain partners (an ownership-type advantage derived from multinationality; cf. Dunning, 1997c). Spreading can therefore also be a strategy to pressure value chain partners (Ruigrok and Van Tulder, 1995). Dispersion allows core companies to avoid 'capture' by other stakeholders. Geographic spread, in other words, can in itself be a strategic asset for core companies.

4.3 Positioning, organization and bargaining relations

Core companies are not solely engaged in non-market activities for the merits of those activities alone. Core company power is related to bargaining power inside and outside the value chain, and bargaining power very much has spatial aspects. As explored in the previous section, tensions within the industrial complex and with governments can induce core companies to pursue strategies of geographic dispersion. The fact that their bargaining partners are relatively more confined geographically means spreading generates increased leverage. Potentially rivalrous relations with other core companies (with potential for greater mobility), on the other hand, are more likely to inhibit spread and precipitate anti-competitive behavior.

4.3.1 Horizontal and vertical positioning

In addition to (and in conjunction with) their internationalization strategies, core companies pursue horizontal and vertical positioning strategies. Core companies can exert distinct influence over chains and sectors by virtue of their positioning. The combination possibilities are endless, but in practice generally only a limited number of alternatives materialize. Figure 4.2 presents five 'archetypal' positioning strategies which core companies can adopt.

Figure 4.2: Horizontal and vertical positioning decisions of core companies

	%value	CHAIN 1	CHAIN 2	CHAIN 3	CHAIN 4
Resources	0				
	10	CORE D	CORE D		
Components	20				
	30				CORE C
	40			CORE C	
	50			CORE B	
Assembly	60	CORE A	CORE A	CORE B	
	70	CORE A	CORE A	CORE B	CORE C
Distribution	80			CORE B	
	90			CORE B	
Consumers	100	CORE E	CORE E	CORE E	

Source: Van Tulder *et al*., 2001

Core Company A: *Horizontal core companies* focus on assembly and/or manufacturing and active in for instance two branches/value chains. A car maker that has diversified into adjacent branches like trucks or trains might be a good example. The competitive advantage of these core firms is primarily related functional excellence, either in manufacturing or distribution.

Core Company B: *Vertically integrated core companies* focus on direct control of a strategic part of the value chain, such as in the chemical and food-processing industries. These core firms exploit competitive advantage in their control over the supply chain, the internalization of markets and product/process innovation excellence.

Core Company C: *Diagonally diversified companies* are positioned in various stages of multiple supply/value chains. Traditional company conglomerates like the Japanese *Keiretsu* are often organized in this way. The competitive advantage for the core firms

arises from the coordination of various activities that might also relate to different product cycles.

Core Company D: *Horizontal resource-based core companies* are situated at the beginning of the value chain. Positioning in multiple value chains is probably required to attain core status, since the risk of substitution effects for firms operating in only one value chain is high. This risk can be mitigated if the resource is strategic and the market oligopolistic, as is the case in e.g. the diamond and gold industry, and in some specialty seeds. The competitive advantage for the core firm comes from the monopoly on a particular strategic input.

Core Company E: *Horizontal retailers* are positioned at the very end of the supply chain. Although sometimes considered a relatively weak position in the past, a number of changes in market structure and competition behavior have reinforced this as a core strategy. The increasing concentration of a small number of companies in this part of the chain, increased horizontal diversification and the change from a sellers' market to a buyers' market due to more assertive consumers have allowed in particular wholesale traders and retailers to reinforce their position. They derive their competitive advantage from their ownership of shops with extensive market reach or as a trading house (such as traditional Japanese *sogo shoshas*) which handle all the exports of a whole cluster of companies.

The more a company moves upstream the value chain, the more its position as a core company can be jeopardized. Other guarantees are required in that case. Either a dominant position in the provision of strategic components or very strong brand value can reinforce the position of the supplier. Intel microprocessors is a textbook case. It not only develops key components, but has also succeeded in convincing consumers (based on a huge advertisement budget) to search for the "Intel Inside" logo. This strategy has changed Intel from a dependent component supplier (of IBM) into a leading core company in the Information Technology business. Computer manufacturers have to a certain degree lost some of their core company status, with the vertically integrated IBM as a prime example.

Positioning strategies also have spatial implications in that the various stages of productive activity and added value, as well as final markets, are not one-dimensional. The ideal-type positioning strategies explored above can in theory be pursued in a single national policy space, or across any number of borders. Moreover, the type of positioning has clear ramifications for a company's bargaining environment since different horizontal and vertical positioning denote different configurations of stakeholders. Key bargaining relations for a company of type 'B' may be with a small number of distributors, while type 'E' will likely interact primarily with a wide range of suppliers. Thus positioning strategy involves bargaining relations.

4.3.2 Core companies and the spatial organization of production

The spatial organization of a core company's activities refers to way in which the production process is organized. Production organization is often associated with Fordist automated assembly, where workers were specialized in a particular stage of the production process instead of each individual good being produced from start to finish by the same worker(s). The crisis of post-Fordism (see Chapter 3) refers thus to the uncertainty in new strategies for organizing production that emerged in the 1980s, just

prior to the time in which the second wave of regionalism was getting underway. That uncertainty was particularly fruitful from the perspective of theoretical development in organization and management, leading to numerous key theories on spatial organization strategies and their organizational consequences (Table 4.3).

Table 4.3: A review of internationalization typologies

	Typologies of internationalization		
	Typology	Characteristics	Organizational aspects
Vernon (1966)	• Domestic • Exports • Some production abroad • Most production abroad	• Production and markets at home • Local sales representatives • Sales offices shift to production • Bulk of production shifts abroad	Organic replication of the organization in host locations
Porter (1986)	• Export-based • Simple global • Country-centered • Highly foreign, coordinated	• Centralized production • Cost-driven production spread • Locally responsive • Centralized, global division of labor	Degree of international coordination
Prahalad & Doz (1987)	• Global • Multifocal • Locally responsive	• Integrated, centralized operations • Balance integration / local pressures • Aimed at diverse markets	Degree of centralization of strategic coordination
Bartlett & Ghoshal (1989)	• Multinational • Global • International • Transnational	• Locally responsive • International assembly • Assembly in final markets • Integrated foreign production	Flexibility to manage tension between local responsiveness and standardization
Ohmae (1990)	• Export • Direct sales / marketing • Direct production • Full autonomy • Global integration	• Exclusive overseas distributor • Wholly-owned local sales company • Local production activities • Local R&D, financing, engineering • Globally sourced inputs, R&D etc.	All forms exhibit highly centralized control internal to the firm
Dekker (1991)	• Local enterprise • International enterprise • Global enterprise • Multinational enterprise • Transnational enterprise	• Produce and sell in home country • Export via local distributors • Limited local production (assembly) • Local production; decentralized • World production centers	Degree of centralization of production
Morrison (1990)	• Domestic • Exporting • International • Global	• No international orientation • Overseas sales / distribution • Efficiency / global responsiveness • High scale, location decisions on potential comparative advantage	Flexibility to manage tension between local responsiveness and standardization
OECD (1996)	• Domestic • Little globalized • Moderately globalized • Substantially globalized • Highly globalized	• Some export • Domestic operations only • Assembly in final markets • Integrated foreign production • Integrated operations in all regions	Degree of integration of production
Ruigrok & Van Tulder, 1995	• Domestic • Export • Screwdriver assembly • Glocal • Regional div. of labor (RDL) • Bi-regional div. of labor • Multidomestic • Global	• Production and markets in home country • Production at home; markets abroad • Final assembly in local markets • Local presence in multiple blocs • Regionally ordered production • RDL in two trade blocs • Autonomous structures in host countries • Globally integrated production strategy	Degree of coordination required (local responsiveness vs. integrated); embedded in concepts of control
Rugman and Hodgetts (2000)	• Export • Overseas subsidiaries • International divisions • Global product • Global area • Global functional	• Centrally coordinated export • Local sales offices • Centralized international operations • Operational responsibility by division • Operational responsibility by area • Responsibility by management function	Major control issues emerge when MNE is truly global. Emphasis on refinement of global typologies, based on division, area or function.

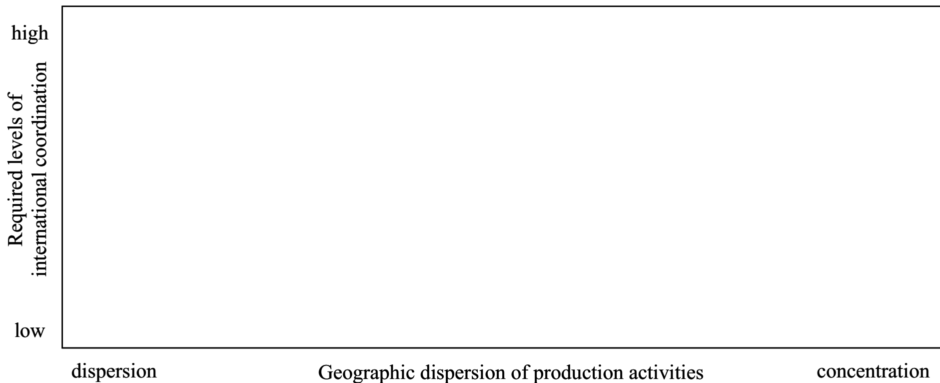
Most of the strategy typologies surveyed in Table 4.3 consider a range of international options described in terms as ‘multinational’, ‘global’, ‘multi-domestic’, ‘international’, or ‘transnational’. In the 1960s and 70s, the primary distinction was between domestic and foreign activity (Vernon, 1966). By the end of the 1980s the key consideration was one of balancing the external demand for ‘local responsiveness’ with the internal demand of standardization, centralization and alignment (Prahalad and Doz, 1987; Bartlett and Ghoshal, 1989; De Wit and Meyer, 1998). Development in this area was relatively stagnant after the early 1990s, with additional typologies limited essentially to refinement of the ‘global’ strategy. Although management typologies of this nature are often criticized as being too ‘dogmatic’ and ignore the ‘space between’ the ideal types (cf. Miller, 1996), they are very useful as a tool for identifying relationships. Miller (p. 506) argues that firms can be clustered based on ‘central themes that align many aspects of strategy and structure’.

With these subtle geographic distinctions, internationalization strategies become less a dichotomous relationship between foreign and domestic, and more an issue of *scale* and *scope* (cf. Van den Berghe, 2003). Scale refers to the overall degree of internationalization of a firm, whereas scope refers to the degree of dispersion. A company can be highly international (high scale), but with all that international activity in one single host country (limited scope). With the same scale, however, a company can have a much broader scope, if for instance its international activity is spread across multiple countries or regions. Scale and scope become particularly relevant in the case of regional integration, whereby not only overall internationalization is a factor, but the configuration of that international activity is central.

In addition to issues of scale and scope (strategy), firms are also faced with issues of coordination and organization (structure). Organization issues refer in the first place to the type or degree of coordination needed to manage that organization (or indeed why that given economic activity should be coordinated by cross-border hierarchies at all instead of markets). While international strategy is usually viewed in a continuum from domestic to globally integrated operations (see Table 4.3), coordination is generally seen as a matter of *centralized decisionmaking* (Ruigrok and Van Tulder, 1995).

A wide range of factors can influence the centralization of decisionmaking within a multinational enterprise, such as size, the intensity of competition, the intensity of innovation in the industry, the homogeneity of product lines, psychic distance between the headquarters and subsidiaries (Rugman and Hodgetts, 2000), as well as the horizontal and vertical positioning strategies described above. Firms can have channels of decisionmaking that are primarily horizontally structured between divisions or branches of activity, but not with higher or lower levels, or be vertically structured, where the chain of command follows the strict hierarchy of the firm. The classic example of different coordination strategies, however, is that of the global versus the multidomestic company. Global integration necessitates an overarching strategy by which all the parts of the whole are linked, while multidomestic strategies involve relatively autonomous, stand-alone operations in individual host countries. Decisionmaking complexity, therefore, is not only a function of greater international scale / scope, but also one of the level of integration with the firm, across borders. This relationship is demonstrated in Ruigrok and Van Tulder’s (1995) conceptualization (Figure 4.3), based on an earlier typology of Porter (1986).

Figure 4.3: Internationalization and levels of coordination



Source: Ruigrok and Van Tulder, 1995: 179

4.3.3 A regionally-relevant typology of strategy

Ruigrok and Van Tulder, in contrast to the remaining typologies presented in Table 4.3, introduce the regional aspect into their typology. A regionally-relevant typology can be constructed that makes the regional aspects of Ruigrok and Van Tulder more explicit and systematizes the multidomestic–integration dichotomy. Almost every core company starts out producing in and for the *domestic* market only (Dekker's 'local' firm). Its operations are concentrated within the national borders and thus require no cross-border coordination. Although sometimes associated with old-economy, protected industries, domestic strategies remained viable for core companies through the 1980s and into the 1990s. Many German core companies for instance, such as RWE, Veba AG and Krupp, have maintained their core positions into the 1990s under primarily domestic strategies. *Export* is often the first form of international activity undertaken, and is usually transitional as some form of production or direct ownership of local distribution in destination markets follows.

The next stage of internationalization involves a shift of production to countries close by, generally in the same (geographic) region. This can be accompanied by varying degrees of cross-border integration. In cases of high tariff barriers to trade, or for firms without a high level of vertical integration, local production may mirror domestic production. This is in essence a *regional multidomestic* strategy. If production is vertically integrated, production may be organized on a regional scale (if trade barriers permit), leading to an ever-increasing *regional division of labor*.

Regionally oriented strategies can also grow into *bi-regional* strategies. In the case of vertically integrated production strategies, firms will have in essence exported their original regional division of labor to a second region such that two parallel and partially complementary production bases emerge (there may even be an attempt to integrate the two regional operations into a larger whole). This is known as a *bi-regional division of labor*. In the case of a multidomestic strategy spanning two regions (the *bi-regional multidomestic* strategy), the firm will have a major hub or national base in each of the two regions and a subsequent number of 'satellite' countries. The hub is a necessary element in

acquiring sufficient critical mass in the host region in which to replicate the multidomestic organization; small piecemeal strategies in a fragmented second region will lack the necessary momentum. In the home region this will be the home country and in the second region most likely the largest market.

Firms whose production strategies encompass more than two regions can be described as *globally integrated* companies. Levitt (1983) is most generally associated with the push for globally integrated strategies, which became a hype that led to the debate on footloose firms and the apparent obsolescence of the nation-state (Ohmae, 1990). At the same time the tension between global reach and local needs created a counterweight to global integration (Douglas and Wind, 1987), reflected in *global multidomestic* strategies ('multinational', Bartlett and Ghoshal, 1989; Dekker, 1991; 'full autonomy', Ohmae, 1990). Global multidomestic strategies are characterized by a high geographic dispersion of activity, but respective national divisions are considerably more autonomous. Unilever is a classic example, with its decentralized structure and locally-sensitive branding strategies and product lines. The global multidomestic strategy is similar to the export strategy in that it may also be the first form of internationalization undertaken by a company. The regionally-relevant typology is summarized in Table 4.4.

Table 4.4: Core company strategies

Strategy	Characteristics
Domestic (DOM)	• Production nearly all in home country • Nearly all sales in home country
Exporter (EXP)	• Production nearly all in home country • Sales considerably more internationalized
Regional division of labor (RDL)	• Production primarily intra-regional • Firm exhibits cross-border integration
Regional multi-domestic (RMDM)	• Production primarily intra-regional • Little to no cross-border integration
Bi-regional division of labor (BiRDL)	• Production is highly internationalized in home region • Production moderately internationalized outside the home region • Extra-regional production primarily centered in a single second region • Firm exhibits cross-border integration
Bi-regional multidomestic (BiRMDM)	• Production is highly internationalized in home region • Production moderately internationalized outside the home region • Extra-regional production primarily centered in a single second region • Little to no cross-border integration
Global (GLOB)	• Production exhibits high geographic dispersion: • Presence in second region as well as third region / rest of world • Firm exhibits cross-border integration
Global multidomestic (GLMDM)	• Production exhibits high geographic dispersion: • Presence in second region as well as third region / rest of world • Little to no cross-border integration

All the strategies described above reflect in large part efforts to deal with institutionalized obstacles to cross-border economic activity (e.g. tariffs, non-tariff barriers, voluntary export requirements) from an insider perspective. The typology omits strategies identified in other studies ('glocal', 'screwdriver assembly') which are typically associated with the Japanese approach to internationalization (Ruigrok and Van Tulder, 1995; Ohmae, 1990). Japan has expressly avoided regionalism as a strategy and hence Japanese companies will

not be considered 'insiders' with respect to any RIA. For this reason regionally-relevant strategy ideal-types are not likely to be characteristic for Japanese core companies and their strategies. As outsiders, Japanese companies are quite relevant, but the outsider-only perspective goes beyond the scope of the current study.

The typology can also be structured in terms of scale and scope into three generic characterizations: low, moderate and high scale and scope of internationalization. Differences between strategy types are in essence a function of a) variations across geographic space ('scale' and 'scope'; cf. Van den Berghe, 2003) and b) variations in coordination levels. Low levels of internationalization are reflected in the strategies of absolutely domestic core companies, whose productive activity is not only produced, but also consumed in the home country, as well as exporters and assemblers, who in essence exploit markets abroad but add little or no value outside the home country. Moderate levels of internationalization include on the one hand the regional division of labor (RDL) and regional multidomestic (RMDM), and on the other hand glocal and centralized transnational strategies, where the latter two strategies imply a (modest) geographic scope beyond the home region. The extra-regionally oriented strategies (bi-regional division of labor, bi-regional multidomestic, global multidomestic and globally integrated) are similarly defined in that their underlying distinction is based on the share of activity outside the home region yet the latter have a more extensive geographic scope. These relationships are illustrated in Figure 4.4.

Figure 4.4: Scale and scope of international strategies

Scale					
	High				GLMDM GLOB
	Moderate to high			BiRMDM BiRDL	
	Low to moderate		RMDM RDL		
	Low	DOM EXP			
		Low	Low to moderate	Moderate to high	High
			Scope		

4.3.4 Organizational complexity through geographic space

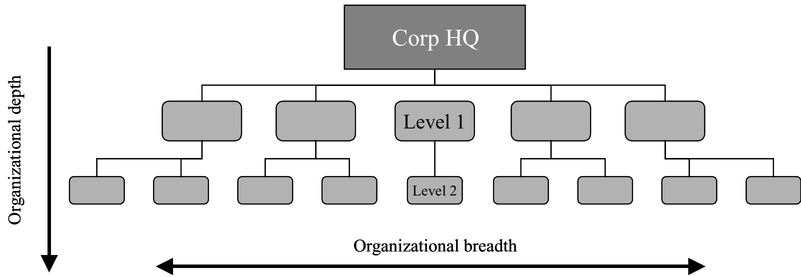
Coordination issues are not only reflected in abstract concepts like decisionmaking or control. Typologies reviewed above like that of Bartlett and Ghoshal (1989) can be used as a starting point for a more physical approach to organizational complexity, focusing on the characteristics of the subsidiary network. Restructuring is considered to have significant implications for subsidiary networks in the form of consolidation, relocation or plant closures. Therefore an analysis of strategic responses to regionalism should encompass not only the degree of *geographic dispersion* but also the *organizational* aspects of that strategy (cf. Van Tulder, 1999).

The 'Network' perspective is commonly used to analyze the internal organization of firms in which subsidiaries are connected through hierarchical as well as lateral relationships. From an organizational point of view, the corporate headquarters can be seen as the place

in which a company's overall strategic vision is formed (cf. Chapter 3) and from which it is disseminated. At the same time it processes flows of strategic information coming up from its subsidiary base and integrates that information into the 'feedback loop' of strategy formation. Moreover, subsidiaries exert a decentralizing force on the control structures of the overall firm, as managers have their own drivers and goals (Birkinshaw and Hood, 1997).

A subsidiary network can also be looked at as a tree, in which depth (vertical decentralization) and breadth (horizontal decentralization) become in themselves measures of complexity. As breadth increases, the complexity of coordinating activity increases. Each 'horizontal' increase in the subsidiary base not only segments the structure further, it creates a possibility for a new branch extending downwards. The narrower the pyramid, the more easily a focused strategy can be maintained. For this reason, first-level subsidiaries are of specific strategic importance. As the depth of the organization increases, new entities are introduced into the whole which require coordination that are increasingly far-removed from the headquarters. Breadth multiplied by depth generates a 'complexity matrix' that demonstrates the overall coordination challenge posed by the company's own organizational structure.

Figure 4.5: Organizational depth versus breadth



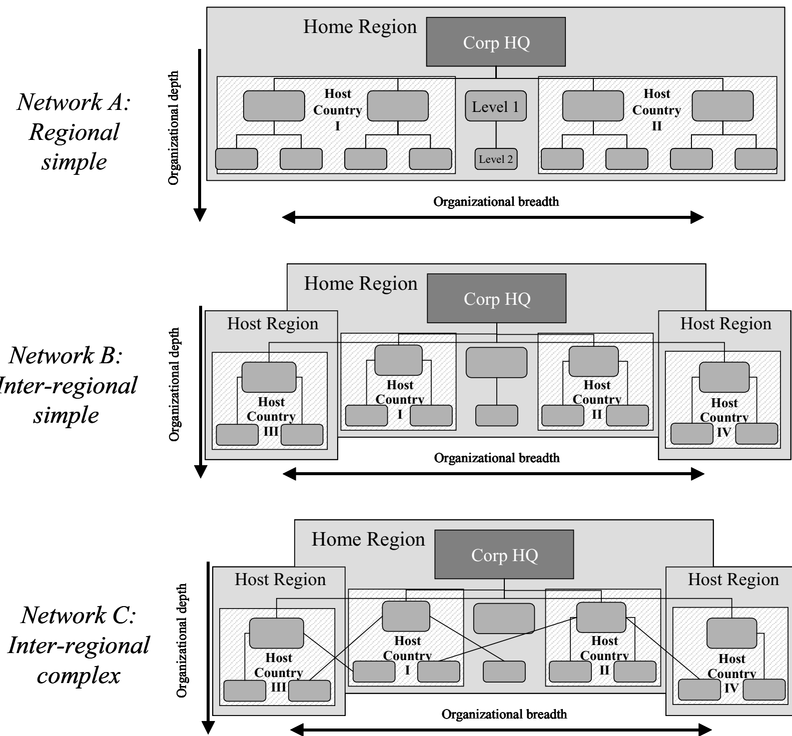
Complexity is also introduced when the structure in Figure 4.5 takes on geographic dimensions. Just as operating in an international environment is considered *ipso facto* more complex than operating at home, introducing the cross-border aspect of relationships between subsidiaries adds an additional dimension to the coordination problem. In terms of individual subsidiaries, the difficulty lies e.g. in the pressures on host subsidiaries to be responsive to local stakeholders, the challenges of integrating foreign (host country) management or shared ownership with host country shareholders.

Cross-border relationships can be categorized at the level of regions as well as individual countries. A regional perspective is particularly relevant for the study of regional integration, because under regional integration, it can be assumed that cross-border complexity is reduced relative to cross-border complexity outside the region. Cross-border linkages between lower-level subsidiaries introduce a third component of organizational complexity. Theoretically each country can be linked into the firm's network through a single direct ownership relationship, where any remaining subsidiaries in that host country all fall under the first. Alternatively, the remaining subsidiaries can themselves be parents

to subsidiaries in other host countries, creating a web of cross-border relationships instead of deep, nationally organized branches. Such a web creates a sort of multiplier effect of scale and scope complexity.

Figure 4.6 shows the ideal-type network in Figure 4.5, but then in different geographic contexts. Network A is a regionally based simple configuration involving only host countries in the home region, where each respective host country is linked by a single hierarchical relationship. Network B has the same breadth and depth as Network A, but is spread over two host regions and a total of four host countries. Network C is identical in geographic makeup to Network B, but adds lateral cross-border linkages. In Network C host countries are linked into the web through multiple ownership relationships, which magnifies the complexity of international operations.

Figure 4.6: Organizational complexity across borders



Regional integration affects firm strategies and can therefore be expected to have various effects on organizational structures. Overall hierarchical depth and breadth may change if companies consolidate operations or rationalize production, e.g. under higher levels of oligopolistic competition. It may also be a flexible response to changes in the configuration of the bargaining environment, e.g. in order to escape the gravitational pull of increasingly regionally organized stakeholders. Consolidation may also involve changes in the number of host countries as well. A higher number of cross-border linkages, meanwhile, may

reflect increased cross-border integration of production, but it could also lead to more extensive control strategies by embedding a firm's subsidiaries in a more rigid (and less transparent) hierarchy.

4.3.5 Internationalization and bargaining power

Although production strategies of course are in part a response to market and demand conditions, spatial organization also plays a key role in managing conflict and bargaining relations (the external equivalent of 'managing interdependencies', Prahalad and Doz, 1987). Ultimately a core company's spatial organization is geared towards preserving its core position through a combination of market and non-market strategies. The division of labor is far more than an issue of labor relations. The way in which a company coordinates its activities (the concept of control, see 4.1.3) involves bargaining relations outside the value chain (in particular with respect to governments) as well as positioning strategies relative to other companies (in particular core companies). Thus 'division of labor' refers to strategies to manage relations at all three levels identified in section 4.2: government, core industrial complex and supranational oligopolies.

The spatial organization of activity has consequences for governments and their relations not only with core companies, but other interest groups as well (see Chapter 3) as governments attempt to exert push-pull forces on firms in the interest of breaking down monopolistic structures, securing job growth or investment growth. A government may therefore have a very different idea of a firm's optimal spatial organization and coordination than the firm itself does (cf. Prahalad and Doz, 1987). Locational decisions at the core company level are also clearly an issue in relations with value chain stakeholders, be they suppliers, customers or labor unions (e.g. the 'divide and rule' tactics discussed in section 4.2.5). A company's spatial organization is, however, also of strategic significance in its relations with other core companies. Supranational (core) oligopolies, and the degree to which inter-firm relations are characterized by collusion or competition, are a major factor in the way core companies choose to allocate production (Table 4.5).

Table 4.5 shows which at which levels bargaining partners are considered *relatively* weak and which *relatively* strong with respect to the core company itself. Where actors are seen as relatively strong are areas of potential conflict and thus levels at which special attention is paid to managing relations. Since the spatial strategies outlined above reflect competitive spaces of varying geographic scope, the other strategic actors in those spaces become increasingly 'diffuse' the greater the international scope of bargaining relations. A company pursuing a multi-domestic strategy, for instance, has to deal with governments in multiple countries while a purely domestic strategy is based on interaction with only the home government. The international character of such competitive spaces has both advantages and disadvantages which are 'balanced out' by the different characteristics of the respective strategies for spatial organization.

Increased economic interdependence and changes in the geopolitical balance of power are related to changes in the configuration of stakeholders and their relative bargaining power. The bargaining relations embodied by the various concepts of control can be analyzed on the basis of the relative strength of the actors in a given competitive space. Relative strength is also a matter of relative threat, and can thusly be related to perceptions of conflict as discussed in section 4.2.2.

Table 4.5: Spatial organization strategies and bargaining relations

International scope of bargaining relations (Low → High)

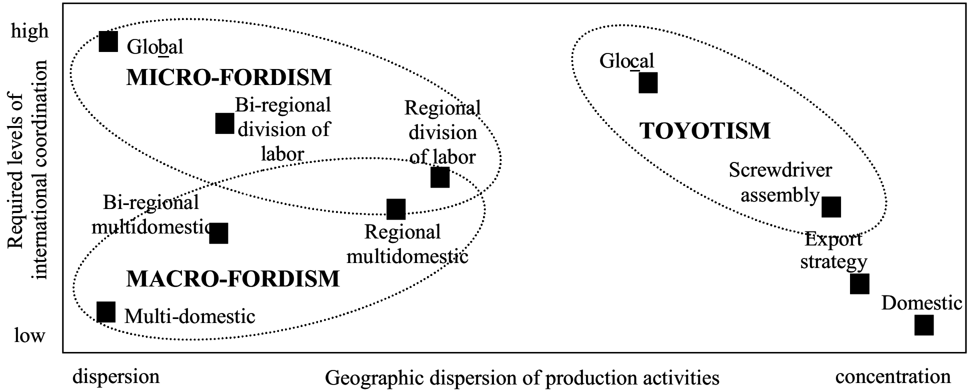
Strategy	*Core industrial complexes*	*Governments*	*Supranational oligopolistic competition*
Domestic	Strong. Able to exert gravitational pull on productive activity	Moderate. Firm has no 'escape' but is also a major player in domestic politics	Weak. No need perceived for international presence
Export-oriented	Strong. Able to exert gravitational pull on productive activity	Strong. Home govt able to effectively restrict 'production leakage'	Weak. No need perceived for international presence
Regional division of labor	Weak. Suppliers and customers played against each other	Weak. Divided by competition for attractive elements of production	Strong. Competitive pressures high in (regional) competitive space
Regional multidomestic	Strong. Local suppliers better embedded in local structures and tastses	Moderate. If markets are fragmented govts can exert significant pressure	Moderate. Depends on the existing supranational character of oligopoly
Bi-regional division of labor	Weak. Suppliers and customers played against each other	Weak. Divided by competition for attractive elements of production	Strong. Competitive pressures high in (global) competitive space
Bi-regional multidomestic	Strong. Local suppliers better embedded in local structures and tastses	Moderate. Pressures to 'localize' necessitate 'insider' behavior. Risk of overstretch and fragmentation	Weak. Competitors tend to be smaller and have less geographic scope
Global	Weak. Production and location decisions based solely on locational / comparative advantages	Weak. Production and location decisions based solely on locational / comparative advantages	Strong. High level of oligopolistic interaction and reaction
Multi-domestic	Strong. Local bargaining partners have extensive influence	Weak. Firms have size and geographic scope to avoid 'regulatory capture'.	Weak. Underdeveloped division of labor only sustainable under low competition

Domestic, export-oriented and multi-domestic core companies share the commonality of being faced with relatively strong labor organizations and value chain partners, while they differ in the degree to which they are able to dominate their relationships with home (and host) governments. Domestic-only core companies do not perceive themselves to be subject to fierce competition in international markets given that their core status is entirely built in the domestic environment. Core companies engaged in export tend to face the same strong partners as domestic companies and share the perception of relatively weak competition, yet find themselves increasingly subject to government demands for export-led growth without 'leakage' of production (i.e., jobs). Strategies with at least a regional level of geographic scope tend to focus on international competition as forming the highest potential for conflict. Production and location decisions are made in response to the exigencies of (primarily cost-based) competition pressures. What differentiates between these strategies is the type of control strategy, i.e. the way in which dependencies are managed, and the way in which that control strategy facilitates varying degrees of internationalization.

4.3.6 Internationalization and concepts of control

Bargaining environments shape strategic choices such that certain strategies are more successful than others under certain bargaining conditions. This does not mean that strategies are solely a by-product of bargaining relations; rather, certain bargaining configurations are conducive to certain types of spatial organization, and that such organization strategies will likely be better than others, all else being the same. Thus we return to the concepts of control explored briefly from a macro-perspective in Chapter 3, section 3. Moreover, the concepts of control emphasize yet again the relationship between bargaining relations and spatial organization (Figure 4.7). Which kind of strategy fits best under which kind of concept of control will be related to the horizontal and vertical positioning choices in 4.2.1, which should in itself give some indication of which kinds of companies are core companies in which countries, and ultimately in which regions.
Figure 4.7 is a snapshot of core company strategies around the mid-1980s, as Fordism in its two variants continued to predominate in the US (micro-Fordism) and Europe (macro-Fordism) yet were subject to declining productivity and, apparently, competitiveness. Alternative strategies were emerging primarily within the Japanese context which appeared to be superior to Fordism. Some Japanese core companies seemed able to outcompete Fordist firms in international markets through simple export strategies (Ohmae, 1990), while others pursued screwdriver assembly.

Figure 4.7: Spatial organization and bargaining environments



Source: Ruigrok and Van Tulder, 1995: 189

Micro-Fordism is characterized by relatively weak bargaining environments in which labor, suppliers and distribution are often fragmented and subject to direct control by the core company. Government is either weak and serves business interests directly, or non-interventionist with a perception of harmonious interests between government and business (e.g., the US and Great Britain). The more internationally dispersed strategies are characterized in particular by relatively weak core network partners who are almost always less international in scope and less cohesive than the core company itself (Cowling and Sugden's [1987] 'divide and rule' strategy). In macro-Fordist environments typical of

Continental European countries, governments and members of the core complex are relatively strong and exert considerable gravitational pull on the activities of their core companies. As a result, core companies in macro-Fordist environments tend to exhibit relatively lower degree of internationalization than firms in micro-Fordist environments. To the extent that they are internationally active, their operations tend to be less centralized in response to the pressures of local (host) bargaining partners. The structural control of suppliers and distribution typically associated with Toyotism is a key feature of Japanese core companies limits the possibilities for extensive internationalization, as structural control is difficult to 'export' to new markets characterized by different pre-existing bargaining environments.

Thus do the typologies reviewed in Table 4.3 clearly betray their 'national' origins. Ohmae's typology reflects the high level of structural control associated with Toyotism at all stages of international activity. Porter (1986), Prahalad and Doz (1987), Bartlett and Ghoshal (1989) and Morrison (1990) show bias towards the micro-Fordist strategies of US multinationals. Morrison's typology, for instance, reflects not only the highly centralized coordination of US companies, but also their attempt to 'export' their production processes in classic micro-Fordist fashion. Perspectives on decisionmaking support these views, albeit from a different angle (Rugman and Hodgetts, 2000). The way in which decisionmaking is centralized is connected to the spatial organization of the firm's activities. Continental European firms, for instance, tend to be fairly decentralized in their decisionmaking, which facilitates the multi-domestic strategy associated with macro-Fordism. On the other hand, the combination of centralized and decentralized mechanisms typical of Japanese firms fits well with the Toyotist precepts of indirect or structural control.

4.4 Core company strategies and regionalism

It is an extension of this logic to argue that the role of European and US core companies in propagating regional institutions (and developing regionalism strategies) is an attempt to find solutions for the crisis of post-Fordism. This section explores possible dynamics in competitive space in response to regional integration in order to highlight how they can differ from the dynamics intended or anticipated by governments. In competitive space, spatial organization is a function both of competitors' relative positions and of bargaining relations both inside and outside the value chain. The locational aspects of regionalism strategies are crucial, because e.g. bargaining leverage in competitive space will be higher with a physical presence in a competitor's market (and access to the competitor's home institutions) than through arm's length trade relationships. Strategies are therefore not necessarily economically driven because core companies have enough power to influence market conditions, distorting the market themselves as opposed to purely responding to it, certainly when it comes to their own competitive spaces. By extention an RIA gives core companies a larger market to distort; outside of that space, they may be forced more into competition-based positioning strategies. Developments of this nature may signal a new type of semi-collusive behavior *within* regions that induces insiders to respect each other's core positions. Core companies, given the strength of their position at home and within their region, may be less likely to see regionalism as an opportunity to expand into the rest of the region as they are to see it in terms of the opportunities it affords for extra-regional

(outward) expansion. Such expansion may be also encouraged if the intra-regional growth dynamic by itself is not sufficient to sustain an insider's core position.

4.4.1 Hypothesized firm-level responses in the literature

Integration can be interpreted on the basis of the literature in different ways. From an internalization perspective, it may be seen as a mechanism that lowers transaction costs and the necessity to internalize. In terms of internalization theory, Regional integration is best seen as a variable that influences the market-versus-hierarchy cost equation and thus the strategic option to license, export or produce locally. As barriers to cross-border activity (transaction costs) fall, companies will either consolidate production in one country and export (final products) or develop a regional division of labor in the case of a vertically integrated company. In addition, firms could develop inter-firm specialization such that each firm produces narrower ranges of goods (Jovanovic, 2001) and trade more with each other (such specialization has collusive qualities in that it signals an inter-firm division of labor instead of competition in similar product markets). Yet, Jovanovic (ibid.) admits, many firms, including car companies, have not capitalized on the potential for concentration of production. Simply put, companies have additional concerns that extend beyond the 'optima' of technology and production curves. Internalization rationale is highly intrinsic and, although clearly relevant, ignores extrinsic considerations of bargaining and strategic positioning.

'Integration has three basic effects on the spatial distribution of economic activity depending on the functional intra-industry production links, the mobility of factors of production and public policy: an industry may either spread or agglomerate, or the regional economic structure may stagnate and polarize in such a way that advanced regions develop high value-added activities and experience low unemployment, while backward regions are left with low value-added economic activities and high unemployment' (Jovanovic, 2001: 3). The choice of RIA strategy, however, is not universal. As Caves (1982) argued, there is no Pareto optimal strategy since options are not always equally attractive or profitable to different firms. Plus, decisions are made at the firm level, not the industry level (Rugman and Verbeke, 1991) and it is not realistic to assume that firms within an industry will react the same way (intrinsic); there are the extrinsic issues of other stakeholders and competitive position.

To take firm-specific capabilities into account, Rugman (1994) employs a 2x2 matrix to analyze the interaction between changes to the policy environment (country-specific advantages) and firm capabilities (firm-specific advantages). Often integration is considered as a risk-reducing phenomenon with (re)location effects on production (Vernon, 1994; Eaton *et al*., 1994). Vernon (1994), considering NAFTA, contrasts short- and long-term effects of integration on corporate restructuring. In the short term, there would be a reshuffling between the three countries as smaller production plants in Canada and Mexico are closed and production relocated to the US to exploit scale. In the long term, however, investment would shift once again to Canada and Mexico as scale opportunities are exhausted and congestion occurs.

Others have generated more subtle, varied hypotheses in contrast to the generalizations of the authors above. Yannopoulos (1990) predicted four basic restructuring responses: 1) defensive import-substituting investment, as extra-regional firms attempt to circumvent regional protectionist tendencies and switch from an export-strategy to local product to

serve the regional market; 2) reorganization investment, whereby firms reorganize production in accordance with regional members' comparative advantages; 3) rationalization investment, where firms respond to scale potential; and 4) offensive import-substituting investment, whereby firms try to capitalize on the growth-enhancing and market-augmenting effects of integration. Buckley *et al*. (2000) categorizes Yannopoulos's original responses in terms of 'insider' and 'outsider' effects. In contrast, other authors assume (in the case of Europe) that outsiders had a better competitive position to start with and therefore 'will be able to appropriate a larger part of the gains assumed to flow from a single market because of their greater initial competitiveness and the fact that it may be easier for them to reorganize' (Young *et al.* 1991: 20).

Such analyses hinge largely on internationalization in the purest sense of domestic versus foreign activity. Foreignness is a matter of political and economic uncertainty and financial risk; regional integration reduces 'foreignness' and thus uncertainty and risk. Yet most core companies have been integrating production internationally a lot longer than RIAs have been in effect (Robson, 1993). Additionally, the firm-level focus in theory development is overwhelmingly investigated empirically with aggregated data. As Buckley *et al*. (2000) point out, 'no disaggregated longitudinal studies have examined the effect of the removal of trade barriers on changes in MNEs' production location decisions' (p. 7). Feinberg and Keane (2001) are a notable exception, using a firm-level dataset to analyze production location decisions of Canadian firms in response to NAFTA.

In the strategy literature, regional integration is viewed as a change in comparative advantage and competitive advantage, in part through raising entry barriers. RIAs are generally associated with the implementation of 'regional' strategies, defined by Morrison and Roth as 'the cross-subsidization of market-share battles in pursuit of regional production, branding and distribution advantages. A transnational corporation 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' (1992, p. 45). Conn and Yip (1997) found that the use of regional strategies was associated with poorer performance, while global strategies were associated with better performance. Schlie and Yip (2000) found in a study of the car industry that global strategy should come first, only possibly complemented by a regional strategy as a second step. In other words, regionalization is not a stepping stone towards globalization. This supports earlier research by the Conference Board which revealed that regionalizing pressures were forcing some companies to 'shift up' to regional strategy, and others to 'shift down' to regional strategy because 'global businesses [were] too cumbersome or insensitive to specific market needs' (cited in Morrison, 1990: 145). Although the strategy literature is very much focused on intra-regional reorganization, it does show that regionalism strategies can be much broader than the adoption of a *regional* strategy.

Third-party (ex-post) studies of the way firms deal with the issue of regional integration emphasize dynamic effects such as economies of scale and product specialization (Single Market Review, 1997; Davies *et al*., 1999; Blank and Haar, 1998). In the SMR study, firms were hesitant to define the SEM as a strategically important issue. Correlations at the national level were higher than for sectors across nations. It is quite likely that many of the firms surveyed did not know with any great certainty what the significance of the SEM would be and may have simply reflected the viewpoints of the 'national' debates. The Blank and Haar study (1998), based on an in-depth survey among North American MNEs

to assess the impact of NAFTA on corporate strategy, found that the North American regional market had become a centerpoint of many firms' strategic outlooks long before NAFTA was ratified. The study, although revealing of firms' strategic perceptions and *intents*, lacked any substantive empirical analysis of real production decisions and as such may be biased towards the 'PR' interests of the companies interviewed.
Davies *et al*. (1999) addressed the issue of competitive pressures and the SEM, assuming that market integration would lead to lower prices, leaving low-cost producers over who would typically increase their scale to exploit scale economies. The survey revealed a definite tendency towards restructuring due to the SEM, namely in a return to core business in response to higher competitive pressures. The study also found that multinationality and diversification are neither substitute nor complementary strategies; i.e., they are both pervasive features of EU manufacturing activity, but a direct correlation is not evident. *Ex-post* studies of this type are based on the underlying assumption that firms are fully informed and respond predictably to market levers. A core company approach is necessary as the very exhaustiveness of e.g. the SMR sample may have led to diffuse responses from firms which either had little stake in an integrated European market or lacked the political vision to know what that stake should be.

4.4.2 Openness from a core company perspective

Under regional integration, the changes to the institutional environment affect bargaining relations with core company complexes, governments, and power struggles within core company oligopolies in different ways. Drawing on Chapter 3, it can be argued that instutitional changes under regionalism can be captured in various dimensions of openness (Table 4.6). The clash between 'integrative' forces on the one hand and those of international diversity can be seen as push-pull dynamics surrounding openness across policy spaces. In fact, regionalism as a political phenomenon can be seen in the context of this 'ideological' debate as an institutional framework within which to address the crisis of post-Fordism.

Table 4.6: Regional openness from a core company perspective

Inward openness		**Outward openness**	
Inside-in	*Outside-in*	*Inside-out*	*Outside-out*
Relations with other insider core companies, regional governments, regional suppliers	Positioning behavior relative to outsider firms, be they core companies, suppliers or customers. Includes non-market strategies.	Extra-regional positioning, relations with extra-regional govts and (potential) core industrial complex partners	Indirect effects on competitive space of third-party core companies and their complexes ('global' competition')

Table 4.6 describes the nature of inward and outward openness from a core company perspective. The inside-in dimension relates to the positioning strategies of core companies with other core companies inside the region, and the bargaining relations with other stakeholders. Outside-in openness (seen from the perspective of an insider core company) relates essentially exclusively to positioning behavior relative to outsider economic actors, be they core companies, suppliers or customers. Outside-in openness regarding political

actors refers to the ability of extra-regional governments to influence intra-regional competitive spaces directly. Although such behavior is possible, it usually follows political channels; therefore core companies will likely manage outside-in openness with respect to outsider governments via lobbying. In terms of outward openness, the inside-out dimension is defined by the positioning strategies of core companies outside the region (both market and non-market). Outside-out openness refers to the (indirect) effects of the regional space on the competitive spaces of outsider core companies and their core complexes. This is, in effect, the impact of core companies' regionalism strategies on 'global competition' and the multilateral system.

The relative importance of different dimensions depends on international exposure of the core company in question. The typology has an explicit 'insider' dimension in that the strategies are considered from within the RIA. The same table, however, could be duplicated to describe the strategies of 'outsiders' (e.g. the response commonly associated with Japanese firms anxious to avoid the prospects of a post-1992 'Fortress Europe'. However, as was suggested under 4.3.4, certain spatial configurations are more associated with certain concepts of control than others, and therefore a given RIA may not be 'home' to the whole range of core company ideal-types. Additionally, it has been suggested that the 'global' and 'glocal' strategies are more ideology than reality and thus only a very select group of firms may be placed under these categories. Which strategies predominate in which given geographic areas, and how these strategies change under regional integration, will be explored at the level of individual regions, and in so doing the typology per region will be more focused. Additionally, changing openness regimes can be expected to affect different strategies in different ways.

4.4.3 Openness and shifting perceptions of conflict

International strategy at the micro level is a matter of geographic scope (Porter, 1986). Responses to RIAs involve shifting resources to gain positioning in response to, and in an attempt to shape, policy decisions and the (re)allocation of rents as a result. Realized restructuring behavior characterizes the outcomes of regional integration trajectories.

Spatial restructuring with respect to any given policy space, or any value chain partner involves location decisions. Core companies like to maintain a geographic spread of activity beyond that expected by efficiency arguments because this allows them to maintain their bargaining position the best. This tendency gains a regional dimension through regionalism pressures, which create and reinforce an 'us versus them' mentality. Just as governments perceive conflict at various levels *in a relative sense*, regionalism shifts perceptions of conflict from the *intra*-regional level to the *inter*-regional level. As a result (depending on the degree to which their competitive spaces supersede policy spaces geographically), core companies may be more concerned with extra-regional strategic considerations.

Hence positioning becomes even more important with respect to extra-regional competitors. As policy space changes, the incentives for companies to locate production within their home country and within their region change. As countries integrate, the size and shape of (potential) competitive space changes, transcending national and even regional boundaries, making issues of outward openness particularly relevant at the firm level. In fact, there is evidence that regionalism creates or reinforces an 'us versus them' mentality among insider firms relative to outsiders. In the North American steel industry,

for example, trade disputes initiated by NAFTA steel producers are increasingly aimed at non-NAFTA producers, with disputes between regional competitors dropping to virtually nil in 1998-99 (Bagsarian, 1999). Of all the 242 WTO disputes in the 1995-2002 period, only nine covered disputes between members of the same RIA. Two applied to NAFTA, in which Canada and Mexico used WTO dispute settlement procedures in 2001 to challenge unilateral positions taken by the United States. Such a move says something about the nature of NAFTA as an institution; consider, again in the case of the steel industry, the US's unilateral 30 percent import duty on foreign steel announced in the spring of 2002.

In the EU, on the other hand, no member country has filed a WTO complaint against another EU member state, which illustrates the advanced nature of EU integration. The 'us versus them' mentality is also given form by the relatively higher threshold under an RIA for outsiders to file complaints. For example, only 13 of the 242 cases mentioned above addressed individual EU countries. Similarly, the European Commission has always acted as plaintiff on behalf of all member countries. 'Us vs. them' is the most logical formula of managing conflict in the context of regionalism and signals in fact a shift towards more extrinsically-driven strategic behavior. Moreover, the us vs. them dichotomy is also a result of institutional changes, as insider firms e.g. have better access to regional capital (national treatment provisions etc.). This makes it a self-reinforcing system.

The example of trade disputes demonstrates that regionalism alters the configuration of bargaining relations within a core company's industrial complex. These bargaining relations are subject to the dynamics of openness in its various dimensions. Different types of openness are more relevant for a given strategy type than others. A domestic firm, for instance, will be primarily affected by inward openness given that its competitive space is limited to its home country. Inside-in openness, or the removal of restrictions to cross-border activity within the region, will likely raise competitive pressures from other regional core companies, as well as potential tensions with home and other regional governments as the opening up of the domestic competitive space threatens the firm's core position. Similar arguments apply if the region is opened up to outsiders, in which case the domestic core company may agitate for special protective measures or resist intrusion by lobbying for dumping charges against the home governments of new extra-regional entrants. If the RIA is designed to 'disentrench' regional core companies by creating incentives to expand extra-regionally, it may weaken the home position of regional competitors as they relocate activities abroad thereby opening up the regional playing field for the domestic core company. Whether the RIA is able to effect some degree of outside-out openness (i.e., openness between extra-regional third parties), on the other hand, will not likely have immediate significant impact.

Core companies employing a regionally-organized division of labor may be more concerned about outside-in openness and the risk of outsiders penetrating their production networks, capturing their suppliers and / or distribution, since an RDL is most effective if the region affords some kind of protection. At the same time, the increased policy harmonization between regional governments and transparency at the policy level will reduce the firm's ability to play regional governments against each other. Some of these risks can be offset by cost reductions afforded by accompanying inside-in openness, but this in turn poses new challenges in the form of less fragmented, regionally-organized suppliers. The ultimate effect may be considerable pressure to relocate extra-regionally. The deeper the integration, the higher the stakes are, and the greater the sense of inter-regional conflict.

Bi-regional firms are faced with an exponential increase in strategic complexity if the regions in which their activities are centered both engage in regional integration. A bi-regional organization runs the risk of being 'torn apart' by the gravitational pull in each respective region and may, particularly in the case of vertically integrated firms (with a bi-regional division of labor), be unable to sustain a cohesive overall strategy. Globally oriented firms, on the other hand, are more likely to have sufficient geographic scope that very few bargaining partners are in a position to exert much pressure, particularly if (as is the case for multidomestic firms) competition often takes place in national markets where competitors are often a fraction of the size of the globally-oriented multidomestic core company.

4.4.4 Migratory internationalization trajectories

As the 'rules of the game' change, strategies can migrate inside the typology grid (Prahalad and Doz, 1987: 30). Strategies are subject to push and pull dimensions in the sense that RIAs may 'push' the behavior of economic actors within the policy space, as well as act as incentives that 'pull' economic actors in other policy spaces. Strategy migrations can be seen as responses to shifts in the nature of a core company's competitive space. Such shifts are characterized by changes in bargaining relations with governments and other stakeholders as well as the degree of exposure to competitive pressures from other core companies. The changed nature of bargaining relations necessitates adaptations to the spatial organization of activity (internationalization) and the coordination applied to that organization. Strategic responses to the new bargaining environment are aimed at reducing the potential for conflict at some or all levels. The security of a core company's core position hinges on its ability to manage these (potentially adversarial) relationships in such a way that its core status is not jeopardized.

The inside-in dynamics under regionalism refer in part to competitive and collusive positioning relative to other regional insider core companies. Positioning depends on the degree of openness and where insider core companies perceive competitive pressures to be intra-regional or extra-regional. If competition is perceived to be intra-regional, internationalization strategies will be part of an effort to deal with that potential competition, as well as changes in the bargaining relations with home governments or partners in the industrial complex. If competition is perceived to be extra-regional, there may be more of a tendency towards collusive behavior within the region rooted in the 'us versus them' mentality which regionalism fosters. Such collusive behavior can lead to a regional 'gentleman's agreement' among core companies. 'The gentleman's agreement' refers to the reluctance of core companies to compete directly with one another in 'a cutthroat way' (Hymer, 1979), and thus to abstain from strategies that form a direct assault on the core networks of other core companies within their home region. This means for instance a lack of initiatives to capture another core company's supply chains, distribution channels, or labor pools. This tacit agreement is rooted in the desire to avoid competition on two fronts; effective global competition strategy would be severely compromised if a core company not only had to compete better against outsiders, but against insiders as well. A more intrinsically driven core company, subject to relatively little conflict with its stakeholders, may develop regional production centers in numerous countries to replace cross-border production chains, consolidating and concentrating individual product segments scattered about the region. Jovanovic (2001), for instance, argues that

horizontally integrated companies specialize production by plant instead of producing all goods in all countries, while vertically integrated companies specialize component production by plant. Such strategies (which Jovanovic attributes to 'increased competition') allow core companies to bundle their strength without sacrificing their geographic spread. This suggests a migration from a multi-domestic strategy to essentially a regional division of labor.

Yet outside-in openness may alter the logic of a regional division of labor because new competitors change the relative costs and benefits of comparative-advantage based production strategies. The entry behavior of outsiders changes the supply and demand characteristics of the local factors upon which advantage is based. Outside-in openness will have the most impact on regionally-oriented core companies (domestics, exporters and RDLs). Although core companies will actively pursue non-market strategies geared towards reducing the possibilities for outsiders to capitalize on intra-regional opportunities, their abilities to minimize outsider penetration directly are limited. If governments enhance import protection for a relatively larger market via integration, this makes the region more attractive for external investors. Through capturing suppliers and distribution channels, as well as labor supplies, core companies can create entry barriers by 'locking up' markets. Additionally, inside-in openness can inherently create entry barriers for outsiders aimed at nationally organized markets because it removes barriers to cross-border activity, forcing entrants *de facto* to compete on a much larger scale instead of pursuing a piecemeal strategy of entering individual national or sub-regional markets one at a time. Meanwhile, insider firms may be able to expand the geographic scope of their industrial complexes as policy harmonization allows for expansion of the core company's concept of control.

Inside-out openness may in itself be a side-effect of inside openness or a matter of active policy stimulation. If the intra-regional competitive space is characterized by anti-competitive behavior and thus precludes aggressive expansion within the home region, extra-regional activity is likely to form the spearhead of growth. Regionalization at the theoretical level would mean a harmonization at certain levels of the bargaining environment, meaning transposition of a core company's control strategy would be better enabled (cf. Ruigrok and Van Tulder, 1995). In other words, expansion is facilitated by regionalism. Extra-regional expansion may in turn be facilitated by outside-out effects of an RIA. Outside-out openness may lead e.g. regional exporters to relocate some of their production outside the region in an attempt to profit from the larger market afforded by the 'me-too' regionalism strategies of its destination market countries.

Companies with extensive geographic dispersion may be forced to agglomerate as value chain partners organize regionally, outsiders raise competition in product and factor markets, or the bargaining power of governments rises as policy is harmonized. Globally integrated firms are more concerned about reduced openness since they are already able to produce effectively across borders and across blocs. Reductions to outside-in openness and outside-out openness may necessitate a retreat to regional divisions of labor, or even glocal strategies. Hence regional openness in different dimensions can precipitate spreading or agglomeration depending on the competitive and bargaining pressures that emerge from altered policy spaces.

Changes to a core company's competitive space may also lead to little or no spatial reconfiguring at all, but that restructuring is limited to matters of coordination. This can amount to new administrative organization, such as the establishment of a regional headquarters or new chains of command. More dramatic alterations can be found in e.g. a

strategic decision to merge, or even be acquired. Merging or being taken over can be 'positive' internationalization strategies in that they form the best option for survival at worst and preservation of core position at best. In other words, a merged or acquired company is not always a 'victim'. Moreover, the opportunities for scale and immediate reduced transaction costs create the possibility for gains by core companies without them actually having to restructure at all. This is particularly derived from a core company's ability to pass the restructuring costs on to other value chain partners. After all, a core company's ability to dictate the terms in competitive space will to a considerable extent determine the degree to which it has to amend its intrinsic strategies in order to compete better.

Certain aspects of strategic behavior as explored here may run counter to the strategic intent of policymakers and their expectations. If RIAs generally lead to de-regionalization of home core companies and increased regional presence by outsider core companies, with their own concepts of control, allegiances and strategic considerations, the changed composition of regional competitive spaces will leave an indelible mark on bargaining in the regional policy space. As a result the engines of growth (and government conceptions of the 'growth regime') inside the region change in composition, building increasingly on the economic behavior and strategies of firms whose allegiances arguably lie outside the region. This has consequences for accountability, bargaining relations in the region and ultimately the legitimacy of the RIA.

4.5 Anticipating the dynamics of Regionalism

It has been established that regional integration involves the push and pull of micro and macro actors through geographic space, and is thus a matter of shifting economic resources. The literature suggests that governments, based on their interests and strategic reality, think more in terms of the domestic and intra-regional outcomes (organization of activity), while core companies think of regional and extra-regional spread of activities. So governments talk of home and host, whereby the emphasis is on regional versus extra-regional host firms, and theory (to some extent) but core companies specifically think about regional versus extra-regional firms, not so much in terms of home and host but in terms of global positioning. The regional aspect is significant because it allows them to enhance market power through e.g. reallocation but also bargaining power through their (collective) government. A cohesive regional government, or at least a regionally shared point of view is more successful in representing and defending insider interests with respect to outsiders than are fragmented national governments (consider the role of the EC in WTO disputes).

The strategic issues embodied in the different levels of perceived tension do not translate to some generic 'region', nor do the core company considerations translate into generic strategies. Chapter 2 emphasized the need to understand realized outcomes in the context of the intended outcomes. Since regionalism strategies are not a uniform concept at either level, a typology of regionalism strategies (a 'strategic repertoire of regionalism') is required. Typologies say something about assumptions of behavior as well as criteria for analysis; in this case strategic intent and realized outcomes reflect issues of power, strategic positioning, anticipated behavior and the spatial organization of economic activity. The core company strategy ideal-types reflect different, distinct combinations of tensions at various levels.

Just as regional integration can be seen in strategic terms as an internationalization strategy employed by states to pace the internationalization of production (Dent, 1997; Ruigrok and Van Tulder, 1995), it can also be argued that core companies pursue cooperative / collusive strategies just like governments do in their policy-level regionalism strategies (cooperation with some countries, increased competition with others), creating a clear macro-micro parallel. On the balance, the ultimate outcome of regionalism strategies may be decreased competition at the regional level, meaning a rent shift towards firms and away from national governments. Furthermore, the outward expansion facilitated by integration spreads firm risk (minimizing effect) *and* rents while policymakers are banking on enhanced bargaining power with respect to companies as a result of increased competition and limiting firms' rent-seeking behavior. Regionalism, therefore, seems aimed at creating room for global competition defined in Porterian terms, but may in fact run in conjunction with regional collusion in Hymerian terms. Predictions of this nature run counter to the logic of market mechanisms in classical regional integration theory and cannot be explained away by an 'invisible globalizing hand'.

4.5.1 The level of analysis problem: two tiers of strategic orientation

The analysis of policy-relevant literature in Chapter 3 suggested that the type of openness explicitly addressed by regionalism policies is overwhelmingly *inward*. Outward openness, on the other hand, is considerably less explicit. Mainstream views of openness look at the extent to which the gains from regionalism can be shared by nonmembers, but do not consider the spatial aspect of those gains. Location is underemphasized because of the focus on trade and the nagging tendency to consider trade and investment (perfect) substitutes. Given the geographically intransigent nature of policy spaces, policies and their effectiveness are measured based on their ability to increase economic activity in the policy space in question. Increasing economic activity can serve either to reduce dependencies on economic activity in other policy spaces (e.g. reduce reliance on imports), or to increase the dependencies of other actors on the economic activity within its own policy space (e.g. increase third parties' dependence on local exports). In either case the increased activity generates improvements in terms of trade and the balance of payments, boosts tax revenues and has a positive effect on jobs and production (Vernon, 1993), which in turn have an impact on sovereignty, policy jurisdiction and ultimately the legitimacy of the state. This consolidation of state power through economic means translates into bargaining power leverage relative to other states.

Openness can be seen from an 'outside-in' (inward) perspective, pertaining to market- and investment access from outside the region, but it can also be seen from an 'inside-out' (outward) perspective, which reflects whether a region is primarily designed to increase interdependence with extra-regional partners or intra-regional partners. For core companies, inward oriented solutions to problems they perceive as outward oriented may be of little value. The assumption that inside-in openness creates a level playing field in each individual member country for firms from all other members suggests that locational concerns are irrelevant. For core companies, location is not only relevant because of cost, price and the availability of factors; the presence of other core companies and the cohesion of their industrial complexes makes a difference. A possible logical outcome of the 'us versus them' mentality is a form of collusive behavior that keeps insiders from penetrating the value chains of other insider core companies and induces them to expand their

competitive space in those areas where they perceive their 'true' competitors to be – extra-regionally. These dynamics may generate outcomes that mesh poorly with those intended by the policymakers. A two-tier approach to the anticipated and realized dynamics of regionalism can contribute to our understanding of outcomes, as well as anticipate the outcomes of future RIAs (Figure 4.8).

Figure 4.8: Two tiers of strategic focus in the spatial effects of regionalism

	Inward dynamics		**Outward dynamics**	
	Inside-in	*Outside-in*	*Inside-out*	*Outside-out*
Policy orientation	← Policy intent? →			
Realized core company restructuring	← Core company restructuring? →			

If, for instance, the policy objective is to shift the balance of power in terms of market share etc in favor of insiders by giving them an advantage over outsiders, an extra-regional growth focus by insiders may undermine that strategy. In fact, it may lead to a situation in which policymakers are faced with a gradually growing 'host' population, in relative terms, as outsiders try to fill in the gap. The result may be a higher degree of 'regulatory capture' (Phelps, 1997) by outside interests with the backing of their home governments, ultimately reducing the bargaining power of the region.

On the one hand, regional integration may induce core companies to seek to expand the geographic scope of their activities. On the other hand, regional integration can be interpreted as an attempt by governments to expand the geographic scope of their policy spaces. Yet the arguments presented here suggest that tensions between the two tiers are related to a tendency at the government level to assume that regionalism policies in fact exert *agglomerating* forces on economic activity, and thus the spatial restructuring of core companies. It can be stated that the deeper the integration, the stronger the 'us versus them' sentiment becomes. Therefore the deeper the integration, the more likely the RIA is to precipitate outside-out effects. Table 4.6 (inside and outside openness) actually reflects the depth of integration: the deeper the RIA, the more likely it is to have inside-out effects and ultimately outside-out (see also Table 3.4).

4.5.2 Core company spaces: collusive or competitive?

If oligopolistic competitive pressures are strong while core companies are faced with (the potential for) conflict on other levels (i.e., strong bargaining partners), core companies may develop strategies to reduce conflict at one or more levels. Managing relations at different levels means that different types of conflict affect a core company's emphasis on collusion versus competition. If a company is particularly engaged in bargaining with government(s), for instance, it may not be desirable or strategically effective to expend extensive resources on 'cutthroat' competition. Depending on the nature of the integration

(depth, perception of adversarial relations at the international level – see Chapter 3), it is possible that core companies will in their strategic focus seek primarily to minimize conflict with other core companies. Such behavior can be expressed in explicitly collusive behavior such as market-sharing, price-rigging or cartel formation, but may also simply be found in a lack of interpenetration in consumer-, intermediate-, or labor-markets (the 'gentleman's agreement') in cases where such interpenetration would seem economically prudent or likely on the basis of e.g. cost calculations and scale potential.

In internationalization processes, core companies are not only competing for destination markets, but for resources and productive assets. As such members of a core company network, particularly suppliers but also e.g. potential employees, become the potential 'stakes' of competitive behavior. Since these assets are to some extent location-bound, internationalization trajectories and division of labor strategies are related to competition between core companies both directly as well as via the dependencies of their bargaining partners. As national economies become increasingly intertwined, it becomes a real strategic issue for core companies how the increased 'exposure' and threat of potential conflict can be managed. In such a case the result may be anti-competitive (collusive) behavior within the home region, possibly combined with an increased sense of competition outside the home region, which brings core companies to shift the focus of their growth and investment strategies outside the region. In other words, if core companies distort markets, an RIA may simply give them a larger space in which to do so; outside of that space, they may be forced into competition in the traditional sense.

Wisse Dekker, at the time the CEO of Philips Electronics, argued in 1989 that the 'SEM is necessary to achieve scale and lower unit costs required for global strategy' (quoted in Morrison, 1990: 144). But scale and reduced unit costs can also be obtained through *reduced* competition in factor markets (monopsonies) between core companies if suppliers are more dependent on their customers than vice versa. A 'gentleman's agreement' can allow core companies to squeeze their suppliers much better because it minimizes suppliers' ability to play core companies against each other. Squeeze can take the form of 'lock in', whereby suppliers are integrated into production such that switching costs are prohibitively high, or by playing suppliers against each other. Lock in is a monopsonist relationship within which the core company can drive down prices, while playing suppliers against each other exposes them to potentially costly uncertainty.

It is thus worth considering the extent to which core companies are by their nature competition-enhancing or anti-competitive (whereby firms can be collusive in one location and competitive in another). What is the role of regionalism? For core companies regionalism is a way to shift conflict and manage bargaining relations more effectively in a more open playing field as precipitated by increasing economic interdependence. The 'us versus them' hypothesis of regionalism (or 'insider / outsider') suggests regionalism could generate increasingly collusive spaces, which would have clear implications for welfare and the distribution of 'rents' in economic activity.

4.5.3 Regionalism and international relations

Regionalism is part of a country's overall positioning strategy and has implications for the distribution of rents across space; i.e., the relationships between governments and regions are at issue. Its outcomes form the basis for measuring the impact and effectiveness of that strategy. Do governments base their expectations on misguided notions of firm behavior?

Regionalism as a policy strategy hinges on heightened growth within the regional policy space. The idea has been that international specialization based on comparative advantage would lead to trade in complementary goods. It is generally assumed that these gains will accrue primarily to insider firms. It is also assumed (or at least, the RIA is legitimated based on the assumption) that trade creation exceeds trade diversion and that investment creation exceeds investment diversion. Nowadays, trade is based on other things, since most goods are available in multiple locations; indeed, many firms produce multiple variations on the same good within single locations. Moreover, investment does not signify increased competition. Both trade and investment can remain intra-firm. It is therefore possible that regionalism leads to an increasing compatibility between policy space and competitive space, except that the latter may be more appropriately designated as 'collusive' spaces.

If so, this has serious ramifications at multiple levels. This has impact on understanding of core company behavior, it says something about the viability of government regionalism strategies. What would that mean for the sustainability and viability for the multilateral system as a whole? If policymakers misinterpret the designs of their core companies, how viable are their growth regimes? If core companies are the linking pins between regions (of various depth/width), do they create pressures towards isomorphism and homogenization, or towards institutional diversity?

The viability of regionalism in the multilateral system may depend on the bargaining relations within the myriad industrial complexes in a given region. Internationalization affects these bargaining relations just as policy changes do. As the policy environment changes, the potential gains and viability of existing internationalization strategies are affected. There might even be a relationship between the depth of integration possible and the pre-existing degree of internationalization of the region's core companies. Alternately, from a core company perspective (including lobbying), regionalism may be an attractive alternative to multilateralism because it limits the number of bargaining partners. Regional integration in terms of 'locking in' is relevant from this perspective as well: this is much more of a risk-mitigating factor than, say, business incentives (cf. UNCTAD, 1998). This frees up 'directly unproductive' (DUP) resources for targeting governments outside the region.

How might the answers to these questions affect future government positioning strategies? What might be at stake in e.g. a battle between China and Japan over the shape and hegemony of ASEAN? What are the risks for the US of pursuing 'unilateral regionalism' in the American continents through the Free Trade Area of the Americas (FTAA), and what role might Brazil and the Mercosur play? Is there a future for regionalism in Africa, and what might be the restructuring impact of true political union in Europe?

4.5.4 The leading research questions revisited

Before proceeding to a more empirical investigation of these issues, recapitulation of the empirical questions posed in the introductory chapter of this study is in order. In cases of the 'second wave' of regionalism, what were the professed outcomes expected by the policymakers? What theoretical arguments and empirical evidence are considered in justifying and substantiating those expectations? What types of strategies do the regional core companies concerned employ? What evidence can be found of core companies' envisioned strategies under regional integration? What kinds of realized restructuring, or

'strategy migration', can be seen? What implicit conclusions can be drawn as to changing bargaining relations in the RIAs under analysis? Do core companies appear to exhibit competitive or collusive behavior? What can we say about the perceptions of behavior between policymakers and core companies? What can be said about the viability of regionalism as an element in international positioning strategies?

PART II:

EMPIRICAL EXPLORATIONS

Just because companies and policymakers share a perception of the stakes does not mean they share the stakes. The micro and macro perceptions of reality relate to the scope of activities within the micro and macro domains. Policy domains are an institutional framework concerned primarily with geographic space within national borders or under supranational institutions (governance structures) within which they attempt to exert influence, or bargaining power. Firms, on the other hand, attempt to exert influence across the entirety of the geographic space in which they operate and compete, which is only determined to a limited extent by policymakers' governance structures. Thus micro and macro domains overlap like patchwork through geographic space, and the location of economic activity becomes a control issue at both levels. Part II of the study is aimed at the search for answers to these issues, and the nature of the approach necessitates keeping the issues within their wider context. Given their complexity, however it would be far beyond the scope of a single study to study them in all their aspects. Areas of focus must be identified in the framework as well as in the dynamics of spatial restructuring.

The focus is on developments after the RIA. Strategic intent is primarily considered in policy space as a way to create *expectations* of restructuring which can then be related to *realized* restructuring *ex post*. The strategic intent of core companies will be dealt with summarily. Instead of developing a 'theory of core company strategy under regionalism', the aim is to expose the diversity in strategic migrations, on the assumption that their strategic behavior flows only *in part* from the intrinsic motives assumed by policymakers. A key assumption is that the strategic behavior of core companies is largely shaped by the extrinsic aspects of maintaining core position in and of itself. In so doing, the analysis will broadly show how the arguments made in Chapter 4 apply. Additionally, the study does not explore the complexities of interaction between core companies and governments leading up to the institutional outcome.

Focus must also be found in terms of the spatial dynamics under study. The openness framework consists of four distinct dimensions for exploration: inside-in, outside-in, inside-out, and outside-out (Figure IIa). For understanding the significance of regionalism, all four dimensions are relevant. Given the firm-level emphasis in this study, however, and the thesis of intra-regional collusion versus competition, the inside-in dimension deserves the most attention. Additionally, the 'us versus them' hypothesis draws attention to the inside-out dimension. To compare possible intra-regional collusion with extra-regional competition, however, necessitates some degree of comparison with the outside-in dimension. For the purposes of this study and the hypotheses laid out in the previous chapter, outside-out is the least important dimension and will thus receive the least

attention empirically. Focus in the spatial dynamics is represented by the darkened blocks in Figure IIa.

Figure IIa: Areas of focus in the dynamics of integration

	Inward dynamics		**Outward dynamics**	
	Inside-in	*Outside-in*	*Inside-out*	*Outside-out*
Policy expectations				
Realized core company restructuring				

Chapter 5 returns to the macro-level to analyze the origins and drivers behind a select sample of five of the key RIAs to have emerged or been institutionalized during the second wave of regionalism in the 1990s. The two most prominent RIAs, the Single European Market (SEM) and the North American Free Trade Agreement (NAFTA), receive the bulk of the attention, not only because of their high-profile character but because of their 'flagship' function and significance for regionalism in the rest of the world. The other three RIAs, the Mercado Común del Sur (Mercosur), the Association of South-East Asian Nations (ASEAN) and the Southern African Development Community (SADC) are relevant more because of their geographic significance, encompassing large swaths of the world's remaining continents and their vast populations, and thus vicariously because of the potential effects they harbor. In addition they exhibit markedly different characteristics than the SEM and the NAFTA, and therefore create a 'foil' against which to juxtapose the latter two regions. At the same time they all look to the NAFTA and SEM as role models to some degree or another and will model their own integration paths based on the observed experiences of the two leading regions. The chapter ends by linking the origins and apparent macro outcomes of these RIAs to the globalization debate addressed in Chapter 2.

In Chapter 6 an overview is given of the world's largest core companies and their spatial organization strategies in the year 1990 in order to provide a context from which to analyze core company restructuring in the decade that followed. The relevant indicators of internationalization and organizational structure are developed and dimensions of restructuring are operationalized. This static view gives way in Chapter 7 to a thorough empirical investigation of core company restructuring. Chapter 8 considers core company internationalization on the aggregate, and Chapter 9 concludes by linking the apparent micro trends with the goals of regionalism in the 1990s, generating conclusions as to the nature and dynamism of regionalism, its place in the global order, on the relationship between government and firm strategic intent and strategic realities, and on the nature of internationalization patterns and 'globalization' at the firm level.

5. REGIONALISM'S 'SECOND WAVE'

Different regions show different motivations with respect to integration and outcomes. This has much to do with the factors shaping the strategic reality of governments, such as development levels, market power, preexisting relations and perceptions of tension with domestic interests and other countries. Similarly, different RIAs may not be predicated on identical views of firms and expectations of their strategic responses. What strategic motives, and inherent assumptions of firm behavior, are evidenced in policy documents of RIAs?

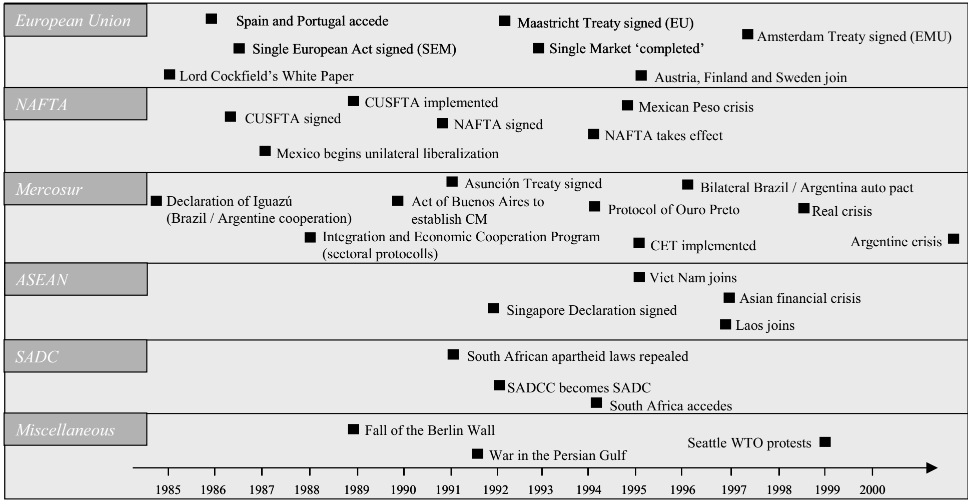
As shown in Chapter 2 (Figure 2.1), the number of RIAs in existence is considerable. For the purpose of empirical exploration the current study focuses primarily on the Single European Market (SEM) and the North American Free Trade Agreement (NAFTA). Although other RIAs were in effect in both Europe and North America during the period under study, the SEM and the NAFTA are clearly politically, economically and demographically the most important RIAs in the world. The Canadian-US Free Trade Agreement (CUSFTA), for instance, implemented in 1991, laid the groundwork for the NAFTA and was essentially 'absorbed' by the NAFTA in 1994. In Europe, the European Free Trade Association (EFTA) lost much of its significance when Austria, Sweden and Finland joined the European Union in 1995, following in the footsteps of Denmark and the UK. The European Monetary Union (EMU) was only implemented in 1999, and at present its restructuring impact is likely to be limited; it therefore falls outside the scope of the present study.

The SEM and the NAFTA are the most well-established and embedded RIAs in the world, and conclusions drawn on the basis of their experience may have bearing on the development of other RIAs. Since they are accordingly also extensively studied phenomena, they may be subject to objections on those grounds. However, they have as yet not been studied in the terms relevant for the current research. The significance of NAFTA is highly disputed seven years after its implementation, and the SEM, despite a wealth of research, shows conflicting outcomes due in large part to the criticisms identified in Chapter 2. Moreover, neither RIA has been studied explicitly from a core company perspective. Those studies which have focused on the role of large firms in the political processes surrounding regionalism trends in both regions have tended not to examine the *ex post* restructuring beyond superficial macroeconomic analysis. These two RIAs, therefore, make excellent case studies for a study of regionalism and core companies, precisely because they have been so exhaustively analyzed without generating clear answers.

It is therefore not the task of the present study to repeat previous studies, but rather to reexamine and reposition the evidence on the basis of the framework laid out in Chapter 3. In doing so a context is created for realized firm strategies in the form of the policy-level strategic intent behind the RIAs, their expectations of firm restructuring and underlying assumptions of firm behavior. First, the SEM is addressed in section 5.1, followed by the NAFTA in section 5.2. After providing a brief overview of the contents of each RIA, each section deals with the RIA's origins in the context of the member governments' policy preferences as conditioned by their perceptions of conflict at different levels. These policy preferences are then translated into their consequences for openness. Subsequently the leading policy models used to predict the RIA's outcomes and legitimate the agreement will be analyzed in terms of their assumed and expected behavior on the part of economic

actors, and how that behavior should contribute to the objectives of the member states. Finally the role, interests and lobby activities of core companies in the region are reviewed before concluding observations are made on the basis of trade and investment data.
However, in keeping with the approach outlined in Chapter 3, these two must be understood in the context of the 'second wave' of regionalism and thus the 'globalization – regionalization' debate in a broader sense. Three additional RIAs have been selected for this purpose: Mercado Común del Sur (Mercosur) in Latin America; the Association of South-East Asian Nations (ASEAN) in Asia and the Southern African Development Community (SADC) in Africa. Not only do these regions show the highest degree of *de facto* integration (other initiatives, such as APEC or TAFTA, are largely on the drawing board), they are also geographically dispersed, reflect different forms of integration, different drivers, logics and each has its own place in the global order. The analysis of Mercosur, ASEAN and SADC will be considerably more restricted as it is primarily intended for input in Section 5.4, which brings together the analyses to compare regionalism in the broader context of multilateral and unilateral strategies. In terms of their institutional development, these five RIAs vary in their intensity but as a group paint a busy picture of integration activity over the 1990s (Figure 5.1).

Figure 5.1: A timeline of the second wave of regionalism



5.1 The Single European Market (SEM)

The EU, as the most advanced integration initiative, is perhaps the most fruitful region for analysis. Some argue, in fact, that the study of European integration has become a discipline in its own right (Bennet, 1997). The characteristics of European integration have been exhaustively studied elsewhere (Molle, 2000; Pelkmans, 1997; Cameron, 1992); here the primary objective is to link those characteristics to the theoretical precepts explored in Chapter 3.

The Single European Act (SEA), approved in 1986 and to be completed by January 1993, was in fact little more than the final stage of implementation of the Treaty of Rome from 1957. Although tariff barriers to trade had been eliminated within the European Economic Community (EEC) as it was then called as of 1968, non-tariff barriers continued to exist in the form of different technical standards, procurement policies and the relative immobility of labor (Bennet, 1997). The central element of the SEA was Article 13, which called for 'an area without internal frontiers in which the free movement of goods, persons, services and capital is ensured in accordance with the provisions of this Treaty [of Rome]' (McDonald and Dearden, 1994: 17). To this end hundreds of measures were taken by the individual member states and common commercial, industrial and social policies have been developed and implemented. The SEM continues to be the centerpiece of European integration, which has since been expanded to formally include more political and economic union.

Although hailed by most as a vital step towards growth and progress in Europe, the European Union has been criticized by others as undemocratic, bureaucratic, and exclusive. It is important to note that the liberalization of trade and investment within Europe by no means implies that the same benefits have been extended to the rest of the world. Hotbeds of contention continue to exist such as the highly subsidized nature of European agriculture under the Common Agricultural Policy (CAP) and the preferential treatment of former colonies in the African, Caribbean and Pacific (ACP) regions.

5.1.1 Policy preferences and realms of conflict

The predominant explanations for integration in Europe are intergovernmentalist or functionalist in nature, while some more recent theories try to blend the two (Moravcsik, 1993; Stone Sweet and Sandholtz, 1997). Functionalist explanations, in which integration is a natural response to increased interdependency, hark back to the post-war period, when faith in technocracy's ability to supersede 'old' national interests was high. The intergovernmentalist approach emphasizes more the purpose of rational heads of state in making an arrangement to deal with collective action problems that ultimately center on security issues. Moravcsik's liberal intergovernmentalism (1993), on the other hand, which attempts to move beyond the limitations of the intergovernmentalist – functionalist debate, has been highly criticized as being too broad and, by trying to capture everything, in fact saying nothing. As such the phenomenon of European integration remains elusive and enigmatic.

The member states, despite their common 'European' character, exhibit considerable diversity in terms of business environment, size, GDP and demographics. Several countries are considered to be the 'core' of Europe: the Benelux, France, Germany, Italy and the UK. European decision-making process has been characterized as 'transnational pluralist', a major departure from some existing national corporatist models (Criekmans, 1998; Schmitter, 1991). That transnational pluralism was and is still focused on the preferences of the core countries as opposed to those of the smaller, economically weaker (and new) members such as Portugal, Greece and Ireland (at the time the EU, or EEC, had only 12 members). Hence the EU can be qualified as a *regional hegemony*.

National differences continue to play an important role, even among the core countries. The UK has traditionally been more open to non-European influences than most continental countries (Casson and McCann, 1999), hence its concept of control is less

"European" than that of the French and that of Germany, whose firms are also proportionately less active outside their home region (Davies *et al*., 1999). In a historical perspective, this relates directly to the post-hegemonic tendency to adopt a stance of open international commerce (Ruigrok and Van Tulder, 1995). UK government might be motivated by a desire for greater global dispersion of UK firm activity. France, on the other hand, might be motivated more by domestic factors like efficiency and growth at home.

Despite diffuse interests on a wide range of issues and potentially incongruous business systems (Whitley, 1998), which some consider a significant barrier to true integration (Ruigrok and Van Tulder, 1995), Young (1991) notes that the tendency to compromise for the sake of unity is particularly strong with respect to foreign economic policy. Although it is plausible to assume that the conditions and the stakes may have differed across countries, the SEM was clearly based on a shared vision. That vision was rooted in a perception of a collective action problem in which countries aspired to collectively enhance the competitiveness of their markets and their firms.

This proposes in essence an inward-looking solution to Europe's problems (Devinney and Hightower, 1991). What was strong enough to precipitate cooperation even when stakes were so diverse and preference congruence was so low? Young (2001) and others tend to focus on the momentum of EU institutions that led to unforeseen cooperation, and the risks of not cooperating, as well as the fact that membership itself alters preferences. These are all inward-looking explanations; there was, however, a more pressing issue: tensions of an extra-regional nature.

The shared vision behind the SEM is best understood in light of 'Eurosclerosis', low productivity, technological backwardness and a country-centered orientation (Phelps, 1997; Young and Hamill, 1992) perceived as sources of weakness compared to firms from other countries, in particular the US and Japan. The assumption was that integration would ultimately lead to more (and cheaper) exports in *third markets* (CEC, 1988; emphasis added). This was in turn based on an assumption that more competitive European firms would raise entry barriers and make it inherently more difficult for non-European firms to compete in the European marketplace (Bhagwati, 1993). In the words of EC Commissioner De Clerq, 'we are not building a single market in order to turn it over to hungry foreigners' (Winters, 1993: 207). Thus the policy preferences were conditioned by perceptions of conflict at the international level, in particular waning European bargaining power relative to the US and Japan (Devinney and Hightower, 1991).

Creating dependence on European exports in third markets generates bargaining leverage for EU governments and at the same time allows them to profit from internal growth in terms favorable for e.g. balance of payments and exchange rates. Thus in the policy-strategic vision, the assumption of intra-regional growth (fueled by rationalization, consolidation and export growth from home markets) engenders rents and terms of trade benefits to EU governments from which they derive bargaining power relative to non-regional countries perceived as competitors.

5.1.2 Openness and the geopolitical positioning of the SEM

Integration in Europe was originally a political mechanism to reduce the likelihood that Europe would ever again be ravaged by war. The very nature of a 'club' agreement creates a perception of inward orientation to the exclusion of others. The SEM's inside-in

openness, embodied in the free movement of goods, labor and services under Article 13, looked like a source of wealth creation to outsiders wanting to get in. The perception of a 'Fortress Europe' was rooted in the function of a Common External Tariff (CET) on the regional borders of the Common Market. As Winters (1992) explains, outside-in openness is governed by three types of trade barrier issues: 1) whether they are revenue raising (through tariff rents); 2) whether they operate on prices or costs (tariffs) or on quantities (import restrictions); 3) whether they are equal to intra and extra trade. Additionally, there is the issue of competitiveness improvement, aimed specifically at EU firms. Yet whether they will be trade diverting or trade creating is unclear, as is how they relate to the trade barrier issues.

It must also be observed that the implementation of the directives aimed at opening up Europe's internal market was not completed by 1993, nor is it fully complete in 2003. On those grounds one can conclude that the EU is not open, simply by virtue of the fact that the greatest exceptions to 'free market' are in sectors in which EU core companies are perceived to be weaker internationally (e.g. autos, telecoms and semiconductors). Real openness would suggest a division of labor beyond the purely regional, yet there is not even a truly Europe-wide division of labor for those sectors.

Hufbauer (1992) concludes that the US will be a minor gainer from 1992 from the extra growth in EU GDP, which would create additional draw for US exports. Some assumed the a priori more efficient outsider firms operating in the EU would be in a better position to capitalize on the opportunities afforded by the SEM (Hood and Young, 1991) and that activities *within* Europe were more important than exports *to* Europe. Hufbauer (1990) predicted that EU competition policy would be favorable to newcomers. In fact, US lobby organizations such as the Business Roundtable were enthusiastic about the opportunities. At the same time, it can be discouraging because the EC will question the activities of outsider firms in Europe. The effects on Europe's trade relations with the developing world, in particular the ACP countries, were also inconclusive. Davenport and Page (1991) predicted diversion of manufactured exports from developing countries, while a Matthews and McAleese study (1990) predicted trade growth. Despite the natural emphasis on outside-in openness, however, Molle (1990) suggests that full (outside-in) openness may not be the best option given that competition is (was) distorted in many markets and thus welfare maximization may be better served by a specific good and factor approach.

Remember that the EU dynamic is not isolated ; there are other things happening too, like the Uruguay Round. EU is not an official actor within WTO, but it acts like one. EC has been an active user of voluntary export restrictions (VERs) against Japan, NIEs, other less developed countries and Eastern Europe. At times, the EC has even argued for legalization of discrimination embodied by VERs but forbidden by GATT. Also, when the US threatened sanctions against the EU in the face of the Iberian enlargement, the British and German governments' responses were clearly calculated on the value of joint bargaining strength (Young, 1991). Young also notes that in certain cases, the interdependence of EU governments can increase a member state's interdependence with the rest of the world. Hufbauer (1990) adds that the EU will not automatically extend reciprocity to third countries unless required to do so.

5.1.3 Policy models and expectations of firm restructuring

The Cecchini report, regarded by many as the ‘official EC view’ of the integration process, summarizes the expectations of integration as follows: direct cost savings due to elimination of (non) tariff barriers; cost savings derived from increased volumes and more efficient location of production (scale and learning economies, and better exploitation of comparative advantage; tightening of competitive pressures, leading to reduced prices and increased efficiency as more firms from different member states compete directly in the bigger market place; and increased competitive pressures leading to speedier innovation. These motivations are supported by others (Oman, 1993; Padoa-Schioppa, 1987). In the words of the Commission itself, ‘in the present condition of the European economy the segmentation and weak competitiveness of many markets mean that there is large potential for the rationalization of production and distribution structures leading to improvements in productivity, and reductions in many costs and prices’ (CEC, 1988, p. 21). Ultimately these improvements would lead to enhanced growth and ‘millions of new jobs’ (Baldwin, 1989: 249).

Policy studies typically employ gravity models and general equilibrium (GE) models to analyze the possible outcomes of the common market in Europe. CEC 1988 emphasizes the use of microeconomic models building on Dixit and Norman’s ‘net welfare gain’ (1980). Models are built on variations across three variables: market structure (ability of firms to enter and exit markets); product ranges (fixed or determined endogenously); and competitive behavior (Cournot or Bertrand) (see CEC, 1988). Yet Winters (1992) cautions that the CEC was a hastily thrown-together study performed by many different economists with different backgrounds and theoretical baggage. The micro-studies at its heart form the basis for partial equilibrium analysis, which in turn forms the basis for the GE models. Baldwin (1989) points out that this is risky business because the assumptions made multiply through the models and can skew the results in ways unanticipated *ex ante*.

The CEC studies reported divergent perceptions as to the largest barriers to growth in Europe. An EC expert commission expected technical barriers to be the biggest obstacle to cross-border activity, particularly in electrical engineering, mechanical engineering, pharmaceuticals, food and tobacco, precision and medical equipment, and after that metal, cars and office machines. The CEC’s business survey showed slightly different results, namely that cars and other transport related machinery were most hampered by technical barriers. These perceptions are predicated on the expectation that larger market size will allow for economies of scale and that ultimately the scale gains will generate technological innovation. The CEC conducted industry case studies on a number of sectors to analyze these assumptions: foodstuffs, pharma, autos, textiles and clothing, building materials and telecom equip. These industries show the most diversity across a number of variables, such as barriers to internal trade, transport costs, economies of scale, technology, homogeneity of tastes, link between internal market policy and external policy, and the significance of government procurement.

The micro models lead to a number of common conclusions. Firstly, there should be greater price competition in European markets. Baldwin (1989), however, warned that reduced profit margins through increased competition may offset the benefits of the larger market (at least for firms, but not for society as a whole). Another overwhelming outcome was the expectation that firms would engage in more cross-border collaboration. In mass-

production environments, concentration and cooperation are expected to be most intense. This would lead to the expansion of activities across Europe.

The microeconomic models used largely ignore strategic concerns (Sachwald, 1993) and make simplistic assumptions about firm behavior and market structure whose applicability to real-world firm situations is questionable (Waverman, 1991). Theories involving increasing returns to scale and profit-motivated technological improvement are empirically unobservable or based on data which is unavailable or unreliable (Baldwin, 1989). The CEC document itself suggests that the dynamic effects of integration may be much greater than the static effects, yet acknowledges that dynamic effects are hard to take into account (CEC, 1988: 37). The major policy studies on the effects of European integration, their assumptions and conclusions are reviewed in Table 5.1.

Table 5.1: Survey of selected policy studies on the impact of the SEM

Policy study	Approach	Assumptions	Conclusions	(Implicit) firm behavior
Padoa-Schioppa *et al.*, 1987	Micro and macro	• Increasing returns • Imperfect competition	• Internal market will lead to price reductions and rationalization • Growth and scale potential should allow European firms to close gap with US firms through increased output and productivity	• Firms will only compete on market principles if they expect govts not to distort markets
CEC, 1988 (Cecchini; Emerson *et al.*, 1988)	Micro; ➔ input for partial equil. macro; ➔ input for GE macro	Variations in: • Market structure • Product ranges • Competitive behavior	• Suggest growth potential but remain ambiguous	• Oligopolists, price takers / price makers • Exploit scale economies • Rationalization
Baldwin, 1989	'New' growth theory	• Endogenous technology growth, • Increasing returns to scale	• One-time efficiency gain multiplies into medium-run growth bonus	• Rational investor • Firms will invest in response to larger market • Firms will improve technology to produce more efficiently
Pelkmans & Winters, 1988	Micro	• Increasing returns • Imperfect competition • Firms must be stimulated to compete 'vigorously'	• Increased variety of goods • Price convergence • Technical efficiency benefits	• Profit maximizing • Higher technological efficiency and cost gains • Specialization • Consolidation
Jacquemin & Sapir, 1988	Factor determinants of intra- vs. extra-regional trade	• Intra-regional trade is intra-industry • Extra-regional trade is inter-industry • Diversification within Europe is vital to growth	• EU members increasingly involved in world-wide division of labor at expense of European Integration • R&D and human capital must be stimulated	• Increasing returns industries will concentrate and export • Capital-intensive high tech industries have advantage

Winters (1992) cites numerous studies critical of the CEC's overly optimistic assumptions. The almost 'religious' emphasis on economies of scale and size (Devinney and Hightower, 1991) does not necessarily reflect the strategic reality of core companies. Additionally, the economic effects of the SEM are not translated into locational consequences for individual firms (Davies *et al.*, 1999; Panić, 1991) and the extra-regional impact remains unconsidered (McDonald and Dearden, 1994). CEC (1988) does contain studies on the

perception of business regarding the costs of non-Europe, but these in no way figure into the final quantification upon which the SEM was 'sold' to the public.

Numerous models are also developed by national central banks to study and predict the impact of integration on national economies. The bulk of these models are macroeconomic in nature and often based on Keynesian assumptions. In the EUROMON model of the central bank of the Netherlands, for example, prices and wages are sluggish, output and employment are demand-determined, prices are simply factor costs plus a mark-up, and wages reflect the bargaining environment (DNB, 1997). Firms' investment behavior is assumed to be a function of macro variables like income, long-term interest, short term interest, change in sales levels, corporate lending rate, cash flow, the GDP deflator, capital utilization, government indebtedness, the liberalization of capital markets and – more generally, the increased internationalization of financial transactions. Exchange rates are also considered crucial: appreciation of the dollar, for instance, leads to higher primary income receipts on dollar investments. Net trade increases as competitive position improves, which is the primary motor for higher GDP.

Such models draw on various theories such as the 'accelerator model', in which investment depends in the short run on acceleration of growth in total sales and on real GDP; from cash-flow and pecking-order theories, in which real profit income also affects investment, and of course neoclassical theory, which predicts decisions based on a comparison of marginal costs and returns that are thus influenced by the interest rate and rate of capacity utilization. To illustrate how sensitive such models can be, the central bank in the Netherlands estimates that a one-percentage point higher rate of capacity utilization is predicted to generate a rise of investment of 0.5 percent in the UK and 2.5 percent in the Netherlands (DNB, 1997).

The firm-level behavior modeled is intrinsic, i.e. rationalization in response to increased competitive pressures. Businesses surveyed also expected exports to other EU countries to increase more than home sales and sales to other countries, but even here the expectations were not that high. A study by the Single Market Review (SMR, 1997) showed that firms Europe-wide were fairly uncertain of the significance of the single market in terms of the opportunities and threats it posed, even *ex post*. This raises the question as to the motives behind the SEM: does the RIA target firms in general, or specific types of firms, i.e. core companies? The ambiguity of business survey results suggest that the vision of a common market that EU governments shared with the business elite may have been targeted more narrowly at that elite than is generally assumed.

5.1.4 The motivations of European core companies

In the bulk of the literature on the European single market program, the role of business, to the extent explicated at all, is subordinated to the role of government. Many authors claim that integration in Europe was purely the result of intergovernmental bargaining (Cowles cites Moravcsik, 1991 and Cameron, 1992), but such explanations are unable to account for the convergence in policy preferences in Europe at the time. Other authors define interests in Europe along business and government lines (Criekmans, 1998). Streeck and Schmitter (1991), for instance, explain that although European business and government elites joined forces in the 1992 project, each did so for their own reasons. European business pursued both market and non-market strategies in defending their interests.

Non-market strategies in essence refer to lobbying. The major lobbyists in the European Union are businesses, which have proven highly effective. Businesses can lobby through various channels, be they members of parliament (MEPs), trade associations, civil servants, professional lobbyists and even the European Commission itself. The European Round Table of Industrialists (ERT), a group of ca. 40 leading industrialists (originally 17 at its inception in 1983), is considered to have a fundamental role in this process. 'The agenda for the Single Market program was largely set by the ERT Through their articulation of the need for European industrial growth and the creation of European-scale projects, ERT members made it clear in direct meetings with government leaders why a unified market was vital' (Criekmans, 1998: 18). This had to do with subsidization of weak industries, restrictive employment practices. By creating more flexibility in their restructuring activities, firms could create economies of scale and (re)create the needed jobs to fuel growth (Cowles, 1995). Scale economies were needed to 'resist pressure from non-European competitors'. Furthermore, 'the European market must serve as a unified 'home' base necessary to allow European firms to develop as powerful competitors in world markets' (1983 ERT report cited in Cowles, 1995: 507)

The underlying assumption on the part of core companies – despite much of the rhetoric – was still that the European market would be relatively protected. In the words of Fiat CEO Agnelli, 'the Single Market must first offer an advantage to European companies. This is a message we must insist on without hesitation' (cited in Bhagwati, 1993: 39). European core companies fully expected political leaders to heed such messages (Greenwood, 1997). The ERT made clear threats to European Commission members that a failure to reach agreement on further integration in Europe would be a clear signal to European industry that growth opportunities were to be sought elsewhere (Cowles, 1995). In other words, ERT members threatened to withdraw from the European arena.

Given the shared perception of poor competitiveness in Europe, a relatively closed region served both business and government power interests. A 'closed' Europe would allow European core-companies to maintain their position in Europe while generating extra-regional activity. In their two-level game, industry expected European policymakers to make the first move, reserving the right to respond accordingly with growth and investment strategies in their own interests (cf. Cowles, 1995). From a policy perspective, the SEM was an inward-looking solution to Europe's waning power. Core companies are also presented as having an inward orientation towards the SEM (Criekmans 1998, Greenwood 1997), with extra-regional growth opportunities in the form of increased export competitiveness.

5.1.5 Trends in European trade and investment

In Europe, policy outcomes in the 1990s more or less followed policy intent – albeit at a somewhat slower pace than hoped for. It can be argued that policy measures surrounding 1992 were enacted with the purpose of achieving the objectives as discussed above, or at the very least that core companies acted on the expectation that this would be the case. Winters (1999): evidence on trade and NTBs in Europe continue to defy simple conclusions. According to Blomström *et al*. (1998), there is no consensus as to the reasons for increased US investment in Europe in the first phase of integration. Dunning (1997a) argues that market size, agglomeration economies etc. were equally as important, if not more so. Most macroempirical analyses, however, are limited to earlier stages of

integration (Barrel and Pain, 1999; Clegg and Scott-Green, 1999), while the current study emphasizes developments surrounding the implementation of the SEM in the early 1990s.
In considering the empirical evidence, it is important to try to link the evidence to the concepts of openness as described in Chapter 3. Two macro-empirical indicators are commonly used to analyze regional integration: trade and investment. In linking these notions to openness it can be established that there are relative and absolute measures of 'openness'. In terms of trade, we can consider not only the ratio of extra-regional to intra-regional trade, which is particularly common in the literature (Clement *et al*., 1999), but also trade as a percentage of GDP, which indicates the overall importance of trade to the region (and can be considered an absolute indicator of the degree of 'openness' of a region) (Flam, 1992). Investment can be analyzed in similar ways, by determining the absolute significance of FDI to the region as well as the relative inward or outward orientation. Table 5.2 presents an overview of trade in terms of exports and FDI as outward stocks, relating both to aggregate regional GDP. World exports and outward FDI stock as a percentage of world GDP (all figures include European data) are provided for reference.

Table 5.2: Trade and FDI trends in the EU15, 1984-2001

	EU Trade		*EU FDI**		*World percentages*	
Year	% of GDP	E/I	% of GDP	E/I	Trade/GDP	FDI/GDP
1984	25.2%	0.70	-	-	23.0%	5.0%
1985	25.6%	0.69	-	-	22.4%	5.6%
1986	22.9%	0.61	-	-	21.1%	5.7%
1987	22.3%	0.57	10.9%	1.63	21.8%	6.2%
1988	22.3%	0.54	11.0%	1.74	22.6%	6.4%
1989	23.4%	0.57	12.7%	1.49	23.3%	7.2%
1990	22.7%	0.52	13.1%	1.20	23.3%	7.9%
1991	21.4%	0.50	13.7%	1.06	23.0%	8.4%
1992	20.7%	0.50	12.5%	1.08	22.9%	8.3%
1993	20.8%	0.62	14.5%	1.05	23.2%	8.9%
1994	22.7%	0.63	15.7%	1.01	24.7%	9.5%
1995	23.9%	0.60	16.0%	0.97	27.1%	9.8%
1996	23.7%	0.59	17.1%	0.97	27.2%	10.6%
1997	25.7%	0.64	19.3%	1.02	27.9%	11.6%
1998	25.8%	0.64	23.5%	1.08	27.0%	14.0%
1999	26.9%	0.62	29.1%	1.06	27.2%	16.0%
2000	29.1%	0.61	-	-	29.6%	19.3%
2001	29.2%	0.64	-	-	28.1%	

*FDI stocks for: Austria, Finland, France, Germany, Italy, the Netherlands, Sweden, and the United Kingdom

First of all, the EU15 can be classified as fairly open based on trade as a percentage of GDP. Moreover, after dipping slightly in the early 1990s (around the time the SEM was implemented), that percentage has risen steadily, from 20.8 percent in 1993 to 29.2 percent in 2001. The way in which trade is 'distributed' around the world shows a different picture, however. The ratio of extra- to intra-regional trade shows firstly that the EU is relatively inward-looking (ratio less than 1). The data also show that after 1992 the EU was slightly more extra-regionally oriented than in the preceding five years. Since the E/I ratio has

stabilized at around 0.6 : 1, it can still be concluded on the whole the EU remains relatively inward-oriented.

This suggests further that the EU was limited in its outside-in openness, because their import values essentially correspond to their export values (i.e., current accounts are more or less balanced). In other words, if the average European country exported largely to other European countries, the average European country also imported largely from other European countries to the exclusion of extra-regional countries.

Despite a lack of reliable FDI data for some EU members over the entire period, it can clearly be seen that outward FDI stock grew considerably in relation to GDP, to a value in 1999 nearly three times that in 1987. Although recent growth is somewhat of an anomaly due to the merger and acquisition (M&A) boom at the end of the 1990s, the preceding years also show steady growth in investment activity. Again, however, that investment is increasingly oriented towards EU member states, although extra-regional FDI stocks continue on the whole to exceed intra-regional FDI stocks.

If the European data are compared to the world trade and FDI percentages, the trade figures exhibit similar values and similar trends. Thus measured in absolute terms, the world as a whole has become more open to trade just as Europe has. In terms of investment behavior, however, the EU is clearly a world leader, with a propensity to invest more than 150 percent higher than the world average.

5.2 The North American Free Trade Agreement (NAFTA)

The North American Free Trade Agreement (NAFTA) was signed on December 17, 1992 by US President Bush Sr., Mexican President Salinas and Canadian Prime Minister Mulroney, to take effect January 1, 1994. The agreement provides for most tariffs between the three countries to be phased out over a 5-15 year period. The scope of NAFTA is limited to trade barriers, and the intensity of integration is low given the absence of a central coordinating body. External trade relations (with third-party countries) remain matters of national policy. Fundamental to NAFTA are the rules of origin (local content requirements) that require considerable shares of the value in final products to have been added in one of the three member countries in order to be eligible for tariff-exempt status. NAFTA is an extension of the Canada-US Free Trade Agreement (CUSFTA), implemented on January 1, 1989. CUSFTA was based on the phased bilateral elimination of tariffs, although its practical significance remains debated. Numerous sectors were excepted, especially in services, such as telecommunications. Additionally, US-Canadian trade was already highly liberalized. The legal scope for bilateral investment, however, was improved in part by the inclusion of a relatively robust dispute settlement procedure (DSP), which arguably reduced the likelihood of either government acting disfavorably towards investors from the other country. NAFTA contains several chapters that reflect separate arrangements between the US and Mexico and Canada and Mexico (USITC, 1993).

5.2.1 Policy preferences and realms of conflict

NAFTA is unique because it is the first case of 'North-South' integration between developed economies and a developing one (Blomström *et al*., 1998). In the past, the idea of reciprocity in trade relations with a superpower was considered by developing countries

to be disastrous (Orme, 1996). But even Canada's status as a developed economy does not put it on an equal footing with the US, which both economically and politically dominates the NAFTA. With the NAFTA effectively creating a $6.2 billion market, Mexico's share is little more than the 'point two', with a GDP roughly equal to that of Ohio (Orme, 1996). In the 23 percent of Mexican GDP in manufacturing, American firms are dominant. According to Pasquero (2000), US interests are much more complex than the improvement of 'national competitiveness' (Hufbauer and Schott, 1993). US president Ronald Reagan was the godfather of NAFTA, and when first discussed it was looked at not just an issue of international free trade, but as a solution to a wide range of problems, such as immigration (Orme, 1996, paraphrasing Martin Anderson, Reagan's first domestic policy adviser in 1979). As a foreign policy, Pasquero (2000) argues that american strategy was fourfold: to reinforce its hegemonic position; to promote its own brand of free-market ideology; to advance democracy through trade and to secure access to world markets. Others, however, argue that the NAFTA is nothing more than a formalization and institutionalization of pre-existing dynamics (cf. Blank and Haar, 1998).

The NAFTA for Mexico was part of a broader effort of openness towards foreign investment, dubbed 'Salinistroika' (Cameron and Tomlin, 2000). Additionally, the NAFTA 'locks in' Mexico's liberalization program and legitimizes Mexican politics (Bosworth *et al*., 1992). Since national economic interests are paramount in foreign policy, the NAFTA may increase perceptions of harmony between domestic and government interests, enhancing the government's legitimacy (Orme, 1996). In part this effort was rooted in Mexico's debt crisis, but also an attempt to force competitiveness upon Mexican conglomerates. Additionally, the NAFTA was seen as a way to protect Mexico against what it views as a highly capricious US trade policy. Mexico's transformation from debtor to creditor made it easier, and a tactically sounder move, to try and talk to Washington as an equal. What Mexico hoped the NAFTA would create abroad was an image of 'new investment opportunities in Mexico and a chance to improve the overall climate of conducting business…not only by lifting restrictions but also by extending various guarantees, for example on the availability for foreign exchange, expropriation and dispute settlement.' (Bosworth *et al*., 1992). As far as Mexican business is concerned, most of the dominant interests are state-controlled. Furthermore, Mexico has never shied away from heavily protecting sectors it sees as strategic and this did not change under the NAFTA.

It is generally agreed that the NAFTA is about the US and Mexico, and that its impact for Canada is minimal (Orme, 1996; Globerman, 1994). Canada was forced to adopt a very reactive position in the integration process. 'For Canada, the negotiations are basically about how to include Mexico in the North American economy, not an opportunity to re-open the FTA or deal with the unfinished American agenda. Canada's basic position is defensive – to protect the [CUS]FTA' (Cameron *et al*., 1992). The legal scope for bilateral investment, however, was improved in part by the inclusion of a relatively robust dispute settlement procedure (DSP), which arguably reduced the likelihood of either government acting disfavorably towards investors from the other country. For Canada, therefore, the NAFTA was more of a defensive measure out of fear of US trade actions. In fact, some argue that the DSPs were Canada's only real gain (Haggard, 1997). Whereas the ambition was originally to diversify trade relations, Canada's strategy ultimately necessitated a focus on the market that mattered most in the face of the US's aggressive unilateralism (Cameron and Tomlin, 2000; USITC, 1993). Canadian business was positive because they saw an FTA as a chance to move away from US production-satellite status. Canadian

industry desperately wanted to develop beyond the 'truncated firm', referring to facilities producing goods (largely for US companies) without the key functions of a 'normal' firm, such as marketing and development.
Perceptions of potential conflict are related to the existing balance of power. As argued in Chapter 3, weaker countries (those with less market power) are more likely to perceive conflict with other (individual) countries, while stronger states are more likely to perceive conflict with supranational blocs of countries. NAFTA was not, for example, a bitter partisan issue in Mexico; most of the opposition came from north of the border. For the smaller two countries, NAFTA was a way to rein in the ability of the US to do as it pleased with respect to trade policy, as both are highly dependent on the US market. Additionally NAFTA was a means to manage their dependence on US host companies which they had fostered ten years earlier. In the US, the NAFTA debate was fought in business councils and editorial boards; the American people were largely ignored.
Supporters argue that NAFTA was part of a broader strategy to enhance national (particularly US) competitiveness by helping local industries compete more effectively against foreign companies at home and secure growth through privileged export access to key intra-regional destination markets (USTR, 2000; Hufbauer and Schott, 1993). The US has not, however, adopted regionalism exclusively. The basic strategy is to press on with multilateralism, while using bilateralism and regionalism where multilateralism fell short, such as the case of intellectual property or services (Haggard, 1997). US felt bilateral negotiations did not interfere with multilateral efforts and would moreover allow the US to exploit its market power to achieve results which would be impossible in multilateral negotiations (Cameron and Tomlin, 2000). Pasquero (2000) points out that between 1993 and 1997 alone, the US signed 245 new trade agreements with its various partners around the world. This diverse palette of strategies and interests means that the NAFTA had an identity crisis from its inception: was it a foreign policy initiative, a domestic jobs program, a pre-emptive strike in coming global trade wars, or an attempt to halt Mexican immigration (Orme, 1996)?

5.2.2 Openness and the geopolitical positioning of NAFTA

In discussing the NAFTA's openness, it should be made explicit that an FTA is in and of itself a fairly shallow form of integration which in part reflects the somewhat divergent interests of the parties involved, but also is better suited to in particular the US strategy of parallel regionalism-multilateralism. Even as an FTA, it is so full of protectionist exemptions and long phase-outs that it 'should be underscored that the NAFTA does not call for free trade' (Globerman, 1994: 23). Weintraub (1992), however, argues that the NAFTA is 'fraught' with GATT provisions and therefore inclined towards a more open regime. Yet Winters (1999) cites evidence that while Canada lowered tariffs on 1500 tariff items following NAFTA implementation, Mexico raised tariffs on 500 items, signaling a less that total commitment to inside-in openness.
In addition to location effects rooted in comparative advantage, the NAFTA introduces effects of a more serious order in the form of the rules of origin. By requiring goods sold on the regional market to be produced, up to a point, using regional production factors (or risk subjection to tariffs), the FTA is by its nature designed to attract economic activity through local content requirements (a form of rent seeking), which were instituted to prevent third countries from using the NAFTA member with the lowest external tariffs as a

portal to access the entire NAFTA market. In fact, NAFTA's local content rules for textiles ('yarn forward') and autos are stricter than they were under the CUSFTA and the NAFTA has elaborate antidumping procedures (Orme, 1996). The three most important changes to investment regulations include expansion to include minority shareholders, the application of most favored nation (MFN) treatment to investments and investors, and new rules and procedures for dealing with disputes in the form of binding international arbitration (Rugman and Gestrin, 1994). Open investment regulations were not imposed upon numerous industries like Mexican oil, telecommunications and the fishing industry (Orme, 1996).

From this perspective, the NAFTA may be – despite the rhetoric – more of a defensive response to the Single Market in Europe (cf. Mansfield and Milner, 2000; Abbot, 1999) by which the US seeks to secure its hemispherical hegemony while Canada and Mexico try to minimize the negative effects this can have. Mexico's new investment law was as much aimed at outside countries as at NAFTA countries (Orme, 1996). Outside-in, therefore, NAFTA was designed to be relatively closed, despite the US government's prevailingly neo-liberal attitude. This is seen by some as a defensive, strategic attempt on the part of the US, in the face of its declining global hegemony, to consolidate regionally and reinvigorate its hegemonial position (Ruigrok and Van Tulder, 1995). Particularly the rules of origin component suggests that NAFTA was designed to be inwardly relatively closed by ensuring that the benefits of tariff reductions will accrue primarily to producers and production in North America (USITC, 1993).

Like Pasquero (2000), Orme (1996) also disputes the assertion that the NAFTA centered on US competitiveness, claiming that its impact in that sense is 'marginal'. It can be said that an overarching goal of any North American trade agreement was to precipitate outward-out openness, as demonstrated by several of the alternatives proposed to the NAFTA. Some tended to favor Strategic Trade Policy (STP) over free trade, while others lobbied for managed trade in favor of tactical protectionism to force open foreign markets. James Baker saw integration as a 'hard-nosed Yankee-trader realism' by which nations reluctant to open their market would be excluded from multilateral progress and at the same time domestic protectionist interests would come under pressure (Baker, 1988 cited in Cameron and Tomlin, 2000).

Mexico's broader strategy for capturing foreign capital, as stated earlier, was not necessarily oriented towards the North American market. Mexico has made clear its intention to extend its free trade and liberalization program in the direction of other regions, particularly Europe. In fact, Cameron and Tomlin (2000) suggest that Mexican President Gortari's decision to pursue NAFTA in earnest was only made once European leaders made clear they did not see Mexico's unilateral liberalization program as sufficient to attract European investment. Also, Mexico is the only country in the world besides Israel to have signed free-trade agreements with both the US and the EU (Economist, Oct. 28, 2000).

5.2.3 Policy models and expectations of firm restructuring

Since the NAFTA is US-led, American arguments and logic predominate. The NAFTA, as an example of north-south integration, hinges heavily on the assumed complementarity of production factors. That complementarity is captured in Hecksher-Ohlin style theory, by which countries will specialize in industries intensive in the factors which are relatively

abundant in that country. The general consensus of the major policy studies was also consistent with Heckshер-Ohlin, generating major gains for Mexico and mild gains for the US and Canada. Globerman (1994) recounts the expectations of the NAFTA as reallocation of resources consistent with patterns of comparative advantage; intensified competition from imports leading to rationalization; DSPs to filter out frivolous attempts at protectionist sanctions; and increased investment by host firms. Moreover, its impact was expected to be 'instantaneous' (Orme, 1996).

Canada's expectations of free trade with the US were based on a lack of 'major evidence that any company, whether favorable or unfavorably disposed, would close up shop in one country or the other on the basis of a Free Trade agreement. That is not to say that it would not happen, but when private companies have been asked by government officials what they would do, the first thought has been rationalization. That would lead one to believe that if a Free Trade agreement were reached, there would not be any massive closings of plants, but plant functions might be considerably altered as companies seek to make use of their new found flexibility' (Nef, 1985, quoted by Blank and Haar, 1998).

Most quantitative studies, particularly the well-known policy studies presented to the US International Trade Commission (USITC, 1993) focus almost exclusively on trade effects of liberalized US-Mexican trade. The bulk of the evidence was generated through computable general equilibrium models (CGE) at the macro or meso levels (see Table 5.3). Partial equilibrium models were employed at the sector level where US and Mexican products are imperfect substitutes (meaning consumers distinguish between domestic and foreign goods) and firms are considered to respond fully to price changes and cost-demand structures. Often aggregate supplies of labor and capital are set exogenously and can flow freely between sectors, respond perfectly to wage differentials, and are always fully employed. Model outcomes depend heavily on estimates of market behavior parameters such as substitution, demand and supply elasticities.

As a result, when it comes down to the specifics, the academic reports were confusing and contradictory (Orme, 1996; Bosworth *et al*., 1992). The USITC admits that applicability of CGE models is 'limited' due to the relative simplicity of the theoretical constructs in relation to the detail of the NAFTA provisions (USITC, 1993: 1-5). In Weintraub's (1992) analysis, most of the benefits reported by the policy models are directly linked to dubious assumptions and the gains are often small enough to be swamped by the 'noise' in the model. Most of the models were constructed prior to the actual details of the agreement and employ divergent assumptions as to e.g. returns to scale, substitutability of foreign for domestic goods and demand elasticities. Rules of origin were omitted from most studies given the difficulty of quantifying these effects in mathematical models. Additionally, many models do not incorporate dynamic effects of increased competition and manifestations of free trade (Globerman, 1994). Therefore, to the extent that CGE models are able to capture the reality of integration effects, they may have operated on the wrong assumptions (see Table 5.3).

Moreover, static CGE models do not predict how labor force or capital stock will change in response to policy, they are therefore unable to predict changes in investment behavior in North America (Gatz, 1997). Faux and Rothstein (1991) argue that the increase in market size (for US firms, by 'adding' Mexico to the market) would be so slight that scale gains would be minimal. Furthermore, the most dramatic effects of the NAFTA generated through dynamic CGE models 'are those that result from increases in foreign investment in Mexico. Yet, in all these models, even in the dynamic ones, this process is modeled as

exogenous' (Bosworth *et al.*, 1992). To assess the extent to which the integration of a small, low-cost country with a group of wealthy countries is likely to affect capital flows, the analogy of EC enlargement in the 1980s has often been used (see e.g. Kehoe comment in Brown, 1992). Comparison with the EC is subject to several problems: 1) rates of growth at the time of accession can determine the overall 'outcomes' of accession; 2) Spain is not the same as Mexico; and 3) US firms wanted into the EU after 1992 out of fear of a 'Fortress Europe'. Meanwhile, Mexico was already one of the most open economies in the world (Weintraub, 1992); investment regimes in Mexico aimed at the US have been virtually unrestricted (in certain sectors) since 1972 (Gatz, 1997).

Table 5.3: Survey of selected policy studies on the impact of NAFTA

Policy study	Approach	Assumptions	Conclusions	(Implicit) firm behavior
KPMG / Business Council, 1991	Static CGE of 44 sectors in each economy	• Variations on investment flows • Production factors substitutes *and* complements • Constant returns to scale	• Negligible rise in US income; trade balance deterioration with Mexico; Mexican gains based on extra flows	• Profit-maximizing • Investment behavior depends on real capital formation and holding of inventories
Hufbauer & Schott, 1992	'Historical' approach: macro and sector analysis	• Continued Mexican liberalization plus increased oil output	• High Mexican GDP and employment growth; modest US employment growth	• As investment is liberalized, firms will shift intermediate production to Mexico
Brown, Deardorff & Stern, 1991	Static CGE using 29 industries	• Increase in demand for labor will lead to greater employment instead of higher wages • Increasing returns to scale	• Positive effects in all three countries with few necessary intersectoral factor reallocations	• Profit-maximizing • Specialization along lines of comparative advantage • Reduced output in response to reduced protection
Cox & Harris, 1991	Static CGE (Canada-specific) for 19 sectors	• NAFTA would mean high barriers against third countries	• Canada suffers little loss from Mexico's tariff-free access to US but gains from competitive effect on Canadian industry	• Rationalization • Cost-based shift towards Mexican suppliers
Hinojosa & Robinson, 1991	Static CGE; 7 broad sectors and 7 comp. static scenarios	• Sector-specific: results sensitive to changes in relative prices and real exchange rates • Constant returns to scale	• Free trade effects small unless part of broader Mexican open development strategy; Mexico gains more than US	• Profit-maximizing • Segment employees on skill levels etc., not on national affiliation
Young & Romero, 1991	Dynamic CGE	• Depends on level of real interest rate in Mexico • Increasing returns to scale	• Substantial GDP gains to Mexico	• Profit-maximizing • Rationalization • Respond to lower price of investment goods

Source: Based on Weintraub (1992) and Brown (1992)

A number of other (partly qualitative) studies referred to by Gatz (1997) focus on sectors, modeling them either implicitly or explicitly. Yet even the USITC (1993) admits that sectoral models cannot capture rules of origin effects. Additionally, policy studies on the impact of NAFTA paid little attention to the extra-regional effects (Globerman, 1994) and tend not to differentiate between foreign markets by dichotomizing the domestic versus 'world' market (Brown, 1992).

Ultimately there was considerably more agreement on the broad expectation that the NAFTA would lead to economic growth. In most cases, the argument was not opposed on its economic merits but on the basis of projected losses to certain sectors or socioeconomic groups. Most were willing to accept that in terms of welfare (at least at the regional level), NAFTA would lead to gains. But the distribution of those gains, the ability of labor markets to respond, and what those gains meant for the restructuring of North American enterprise, were highly disputed. Faux and Rothstein (1991), for instance, argued that at a point when US industry is at a crossroads between a high-skills, high-wage path (innovative, high-quality goods saleable at margins high enough to support US living standards) and a low-wage, low-skills path (cutting labor costs), the FTA embodies a choice for the latter. Orme, meanwhile, argues that the NAFTA calls for 'replacing low-wage sunset industries with high-wage sunrise industries.' (Orme, 1996: 3).

5.2.4 The motivations of North American core companies

Given the micro-Fordist environment of US firms, the NAFTA is very much a firm-led integration agreement. Many US companies have propagated the view that North American integration was a reality way before the NAFTA that according to one executive 'it almost makes the agreement secondary' (Blank and Haar, 1998). It is therefore not surprising that the managers surveyed for the Blank and Haar study (1998) identified NAFTA with the emergence of a continental economy rather than more narrowly with the legal accord itself.

One of the important aspects of NAFTA is that core companies, whose behavior is at the root of the policy debate and whose role in the agreement itself is undeniable, are essentially only located in the US. Canadian opponents were concerned that NAFTA would lead to US firms repatriating capital to the US, consolidating their operations and reducing investment and employment in Canada. Mexican opponents were concerned about the ability of Mexican companies to compete? The saga of Mexican steel producers and the barriers set up by the US in the early 80s taught Mexican planners that leading industries must always be ready to shift markets quickly, and that these shifts are only feasible within NAFTA. Firms expected that continent-wide integration would give them much more flexibility to shift production within corporate networks (Blank and Haar, 1998).

To one observer, the NAFTA is 'clearly a political agreement that helps institutionalize the rent-seeking behavior of US core companies by positioning [political] matters such as unlawful dismissal, the right to strike and emissions standards as fundamental trade issues' (Globerman, 1994: 23). In an environment characterized by power asymmetries between firms and governments (Rugman and D'Cruz, 1994) the interests of particularly the US automotive industry came to the fore (Hufbauer and Schott, 1993). The Big Three US automakers (Ford, GM and Chrysler) exploited power asymmetries to the detriment of the foreign competition, effectively kicking Japanese auto manufacturer Honda (with its large North American presence) out of the North American Auto Manufacturers' Association on the basis of its divergent NAFTA standpoint (Hufbauer and Schott, 1993).

The antagonistic relationship between core companies and governments makes the 'shared vision' among North American core companies in the case of the NAFTA different from that of European core companies in the EU. Whereas EU companies were more vocal about the use of protectionist (non-tariff) barriers to safeguard their own positions, US

companies in particular were adamant about limiting the use of such potentially powerful weapons by Canada and Mexico. The Chapter 11 provisions, for instance, which allow regional firms to lodge complaints against governments perceived as being discriminatory, was a vital ingredient North American core companies agitated for. Recent critical reports (cf. IISD-WWF, 2001) suggest that these provisions may be used as a weapon to undermine legitimate regulation – particularly environmental and natural resource management measures. As of March 2001, 10 out of a total of 17 NAFTA Chapter 11 cases have been brought against such measures.

Corporate proponents expected NAFTA to be a win-win situation. Rapidly expanding markets in Mexico and rising levels of demand for a wide range of products were expected to lead to a substantial increase in production in Mexico and ultimately Mexican export growth (Blank and Haar, 1998). At the same time it was predicted that increasing consumption and rising purchasing power in Mexico would ensure that production and employment in the US and Canada would not suffer. In some cases this would concern Mexico's potential as a destination market (Orme, 1996), and others were more interested in exporting (back) to the US. 'We clearly want to export more to the US, particularly higher-end production, since certain product lines are still cheaper to import from Asia than to manufacture here or import from the US' (Garen Chu for Singer Mexicana, interviewed in Blank and Haar 1998).

US core companies were quick to propagate the win-win angle. One loose-knit organization, 'USA-NAFTA', was formed by the CEOs of 35 of America's largest corporations (including e.g. Kodak, Xerox, GM, GE and AT&T) to actively lobby both politicians and the public (through the media) to drum up support for the agreement (Public Citizen). US companies saw in the NAFTA a 'blueprint for the more efficient reordering of industrial production on a continental scale' (Orme, 1996: 4). IBM began consolidation and reorganization involving centralization of business units in 1990, by which Canada, the US and Mexico would fall under IBM North America. 'As a response to the increasing number of customers that have been demanding cross-border devices, IBM will become as seamless as possible across North America…If your customers are organized on a North American basis, we have to organize on a North American basis too' (John Akers, former CEO IBM (Blank and Haar, 1998). According to Pablo Rosales, the General Director of Honeywell, Mexico, 'reevaluation of the Mexican market caused a 180-degree turn in the firm's thinking. 'Global thinking' is the centerpiece of our new, corporate culture, and Mexico's potential is tremendous' (Blank and Haar, 1998).

US business lobby organizations by and large adhered to the mainstream economic logic. The KPMG Peat Marwick study referred to in Table 5.3, for instance, was commissioned by the pro-NAFTA Business Council. The rationale behind integrating operations was to increase profitability, increase market share, and reduce overhead. The most important factors in determining strategy were: globalization, international competition, growth potential, product development / change, and changes in competitive advantage. When asked which areas of operations had been subjected to significant change in response to NAFTA, 44 percent of respondents said scale of production, 35 percent mentioned new production opportunities, 29 percent said marketing, and 27 percent indicated the degree of product specialization / sophistication. 'Location' was mentioned as an area of significant change by only 21 percent.

Yet in several companies, such as Kodak, the Mexican subsidiary continued to report to the firm's Latin American division. Strong personal feelings as well as organizational

concerns inhibited major changes in structure. Motorola, meanwhile, found that it benefited from keeping Mexican operations under its Latin American umbrella. Mexican management in this case believed that its Latin American customers appreciated a strong Latin orientation; the firm was reluctant, therefore to integrate its Mexican operations into a North American operation. All of thee reasons made integration into a North American business unit more difficult in practical terms, however desirable in theory.

5.2.5 Trends in North American trade and investment

The macro data reveal that NAFTA constitutes a relatively closed region with less than ten percent of the combined GDPs of the United States, Canada and Mexico traded (Table 5.4). NAFTA's traded share of GDP has been slowly but steadily rising since the midst of the 1980s, in particular during the years immediately following implementation of the NAFTA. That growth has been tempered in recent years and even declined in 2000 and 2001. Overall, a trade to GDP ratio of 1 to 10 is quite low, as will be evidenced after comparison with other RIAs to follow, but is not surprising given that the bulk of activity takes place within the US domestic market and clearly does not qualify as trade.

Table 5.4: Trade and FDI trends in North America, 1984-2001

	NAFTA Trade		*NAFTA FDI (stock)*		*World percentages*	
Year	% of GDP	E/I	% of GDP	E/I	Trade/GDP	FDI/GDP
1984	7.9%	1.42	5.9%	1.91	23.0%	5.0%
1985	7.2%	1.32	6.0%	1.97	22.4%	5.6%
1986	7.0%	1.46	6.5%	2.13	21.1%	5.7%
1987	7.3%	1.33	7.3%	2.40	21.8%	6.2%
1988	8.3%	1.47	7.3%	2.36	22.6%	6.4%
1989	8.4%	1.47	7.6%	2.55	23.3%	7.2%
1990	8.6%	1.40	8.1%	2.67	23.3%	7.9%
1991	9.0%	1.37	8.5%	2.82	23.0%	8.4%
1992	9.0%	1.30	8.5%	2.99	22.9%	8.3%
1993	9.1%	1.19	9.1%	3.27	23.2%	8.9%
1994	9.6%	1.10	9.4%	3.18	24.7%	9.5%
1995	10.9%	1.17	10.4%	3.37	27.1%	9.8%
1996	11.2%	1.11	11.3%	3.51	27.2%	10.6%
1997	11.5%	1.04	11.7%	3.42	27.9%	11.6%
1998	11.0%	0.94	12.8%	3.56	27.0%	14.0%
1999	11.0%	0.91	13.6%	3.70	27.2%	16.0%
2000	10.9%	0.79	13.3%	3.60	29.6%	19.3%
2001	10.2%	0.83	-	-	28.1%	

At the same time the share of intra-regional exports relative to extra-regional exports steadily increased. This effect could be noted already before the formalization of NAFTA in January 1994. The 1995 rise to an E/I value of 1.17 from 1.10 the previous year is related to the Peso Crisis in Mexico and the denomination here of trade in US dollars, which reduced both the nominal value (through reduced Mexican demand) and real value through Mexican depreciation) of the Mexican component of NAFTA trade. As overall

trade volumes stalled in the late 1990s, the E/I ratio plummeted to below the balance line, indicating that a decrease in extra-regional trade was primarily responsible for the stagnation. Thus the macro (trade) dynamics of regional integration after NAFTA have been towards increased closedness.

Furthermore, the country-level data underlying Table 5.4 show that all of Canada's export growth after 1995 is due to increased exports to the US. There is also a NAFTA trade deficit; i.e., more trade flowing into the US than from US to Canada and Mexico. This aggregate trade deficit reflects the US running current account deficit, which is largely financed by attracting inward investment.

As indicated in preceding sections, policy studies on the impact of the NAFTA have centered on foreign investment effects, particularly inflows to Mexico. The trade picture is paralleled by the absolute investment position (as a percent of GDP) of the region, being relatively closed and in comparison to for instance the European Union). The outward FDI position of NAFTA countries, however, is considerably more extra-regionally oriented than its trade activity, while extra-regional and intra-regional FDI positions are relatively balanced. For every dollar of intra-regional outward FDI stocks in 1984 there were almost two dollars positioned extra-regionally, and that disparity has nearly doubled since. The value of extra-regional outward FDI stock is now more than 3.5 times that of regional outward FDI stocks.

As Blomström *et al*. (1998) suggest, the increased investment in Canada which paralleled the increase in trade from Canada appears to support contentions that much of US-Canada trade is intra-firm. The Canadian government, using US Bureau of Economic Analysis (BEA) data, concluded that 40 percent of all Canada-US trade in 1998 was intra-firm (Industry Canada, 2001). That intra-firm trade is primarily a result of US firms investing in Canada and then exporting those (intermediate) products back to the US, or the export of intermediate goods to Canada for further processing and reimport into the US.

One must exercise caution in interpreting such data, because they clearly reflect other influences than simply the implementation of free trade policies. Still, Blomström *et al.* (1998) and others characterize the trade and FDI trends as weaker than expected, which would appear at odds with the rhetoric of regionalism captured in the interviews of Blank and Haar (1998).

5.3 Other manifestations of regionalism

In this section the analysis will be considerably more superficial as it is intended to provide material for comparison for the two main regions under study. It draws largely on Ten Napel, 1998.

5.3.1 Mercado Común del Sur (Mercosur)

Under the Treaty of Asunción, signed on March 26, 1991 by the Presidents of Argentina, Brazil, Paraguay and Uruguay, the Mercado Común del Sur (Mercosur) was established. Mercosur stems from the earlier Integration, Co-operation and Development Treaty of August 1989 between Argentina and Brazil, which in turn was based on the Iguazú Declaration of November 1985. The treaty was subsequently ratified by all members and entered into force on November 29, 1991. The Treaty of Asunción has been formally amended once, in the Additional Protocol of the Treaty of Asunción, known as the 'Protocol

of Ouro Preto', signed on December 17, 1994. This protocol, which concerns mainly institutional issues as well as dispute settlement, is also considered to confer on Mercosur a distinct international legal personality.

As the name shows, Mercosur is designed to be a common market. The Treaty of Asunción foreshadowed the establishment of a common market among the four countries with free circulation of goods, services, capital and workers from January 1 1995 (but not all of this ambitious program was achieved). The treaty has 25 Articles in six main chapters covering the purposes, principles and instruments of Mercosur, the organizational structure, the period of application, accession, denunciation (withdrawal) and general provisions. In addition, there are annexes covering the trade liberalization program, rules of origin, dispute settlement, safeguards (including against other members of Mercosur), and the establishment of technical and policy working groups. Safeguards follow the guidelines of Article XIX of the GATT, but these have not been allowed on intra-regional trade since the beginning of 1995. The broad principles for dispute settlement were set out in the Treaty of Asunción. Various stages and procedures were elaborated in the Brasilia Protocol for the Settlement of Disputes, signed on 17 December 1991, and this is maintained in accordance with Article 43 of the Protocol of Ouro Preto.

Brazil is the economic powerhouse, accounting for 75 percent of Mercosur's GDP and 80 percent of its industrial manufacturers (Mattli, 1999b). Until 2001, Argentina was the more stable of the two economies, with a currency peg to the dollar ensuring a stable macroeconomic environment. Yet Brazil has failed to assume its leadership role, opting for short-term national interests over regional ones. In the early 1990s Mercosur would have likely been characterized as a dual hegemony under Brazilian and Argentine leadership, but squabbles between the two and the economic crises that gripped the region from the late 1990s on have made any kind of policy coordination next to impossible and considerably reduced any real likelihood of further strengthening of integration. Mercosur's integration process has also stalled in part due to the prospect of a pan-American FTA (the Free Trade Area of the Americas, or FTAA). In particular Brazil seems to expect the FTAA to bolster its regional hegemony and thus appears to have adopted a wait-and-see attitude.

As is generally the case in developing countries, regional economies are corporatist-statist with deeply entrenched monopolistic and/or oligopolistic market structures. Liberalization processes already underway prior to Mercosur were designed as an outward-oriented growth strategy, in contrast to Import-Substitution Industrialization (ISI). There is considerable merger & acquisition (M&A) activity; home core companies are under constant threat: if they do not do well, they fail, and if they do too well, they are simply bought up. Therefore many home core companies are either being transformed or faced with glossy new competition, and there is a risk of concentration of power in the hands of host firms. In this light competition policy is particularly important, particularly where it might seem that host firms are better able to capitalize on the opportunities provided by integration.

In Mercosur the idea was for Argentina to raise tariffs on imported capital goods to meet Brazilian levels, which suggests some level of 'closedness'. In the case of integration depth, however, Mercosur integration has been subordinate to the relations that each country maintains with its main trade partners. With the exception of special cases like Bolivia, Paraguay, Uruguay and Argentina, the main trade partners have not been, or are not, countries in the region. In some circumstances the integration process has served as a

support instrument to achieve national objectives which were shared by two or more countries. This has been the case of Mercosur to date. The President of Uruguay expressed this in a conference given at SELA in March 1997: 'What was attempted with Mercosur were basically three objectives: the first was democratic consolidation which was the priority at that moment. You realize that priorities change with time: in 1985, the priority was political, then it became economic and today we feel it is social.'

Although Latin America is most often clustered under the American 'sphere of influence', Mercosur was modeled more along European lines. According to Luis Rubio, President of the Center of Research for Development (CIDAC) in Mexico, 'while Mexico, Central America and the Caribbean look to the US and NAFTA as a trade model, South American countries are closer to Europe culturally and have established Mercosur along EU lines to a certain extent.' Mattli (1999b) describes Mercosur as a response to the end of the Cold War and changes in Europe that led more towards an inward orientation, coupled with Mexican president Salinas's intention to seek a free trade pact with the US. Mattli describes Mercosur in this context as an example of reactive integration, in which countries enhance their cooperation due to perceptions of external change (largely in response to other RIAs). Latin American countries on the whole were seriously afraid of being less of a priority in Europe's eyes. On the one hand was the fear of investment and aid diversion to Eastern Europe, on the other the exclusion of Latin American trade. In particular the role of Germany as the lynchpin in EU–Latin American relations was a cause for concern in the wake of German reunification.

5.3.2 Association of South-East Asian Nations (ASEAN-FTA)

The Association of South-East Asian Nations dates from 1967 and was primarily politically motivated, as a counterweight to the instability in Indochina at the time. ASEAN was very much an anti-communist initiative taken at a time when the US and Great Britain began to signal a retreat from Southeast Asia. The focus of its founding members (Malaysia, the Philippines, Thailand, Indonesia and Singapore) was to maintain peace and stability in the region by providing a forum for the discussion, maintaining open channels for dialogue and resolution of potentially destabilizing issues (Boudhan, 1997).

The FTA was a longer-term goal; not until 1993 was there a Common Effective Preferential Tariff (CEPT). First steps were taken in 1976 at the First Summit meeting, where aims of enhancing economic growth and social development were expressed, although security issues remained prominent. The Concord signed at the First Summit identified four major areas of cooperation: cooperation in basic commodities, particularly food and energy; industrial cooperation; cooperation in trade and joint approach to international commodity problems.

With the accession of Brunei in 1984, Vietnam in 1995 and Laos and Myanmar in 1997, the group's diversity in terms of openness, growth and development levels increased greatly. Singapore, Malaysia and Brunei, for instance, are open, outward-oriented market economies, Indonesia is highly protected and three of the members (Laos, Vietnam and Myanmar) are totalitarian or planned economies. As a result, integration has been relatively shallow and selective. Its economic basis is threefold: selective trade liberalization, industrial complementary agreements, and allocation of major industrial projects. There is no centralized decision-making and policy formulation is left to each

individual country. It is important to realize that ASEAN is not based on a treaty like other regions are; bargaining in ASEAN is therefore informal.
Currently only a preferential trade area (PTA), it was decided at the Fourth Summit in Singapore in January 1992, to establish an ASEAN FTA within 15 years. The Singapore summit emphasized a commitment to open regionalism. This is logical in the context of the East Asian Miracle transpiring at the time, in the form of exorbitant growth rates and booming exports. The rationale for industrial cooperation was based on the expectations of a larger combined market and economies of scale. Specialization in niches of specific value chains and enhancement of investment climate. Underlying premise: export-led growth.
Economic growth in the region was not initially linked to liberalization. Industrialization began under protectionist ISI strategies and, although views have become more liberal over the 1990s, most ASEAN countries have a penchant for regulating trade and investment. Nonetheless, in particular the core ASEAN countries in principle welcome foreign investors and have developed several incentive packages to attract more FDI. These incentives include provisions for foreign ownership, for export-oriented FDI, permission for export-oriented firms to distribute domestically, and allowing joint ventures to participate in government exports. At the same time, the CEPT scheme calls for foreign companies to meet a 40 percent local content requirement in order to trade their products in ASEAN (UNCTAD, 1996: 106-109).
Yoshida *et al*. (1994) describe ASEAN as a typical case of market-led integration, associated with 'positive' integration. The US has long promoted increased openness in Asia, but although ASEAN to some extent reflects the policy interests of the US, one must recognize that the US has to contend particularly with Japanese influence in the region, whose policy agenda does not overlap with the US (Haggard, 1997). The struggle for dominance in the region is related to the absence of a clear leader within ASEAN. As a result ASEAN is generally qualified as being externally dominated, with Japan as the primary external hegemon. One of the reasons Asia is not further integrated under Japanese tutelage is because of the US's economic and military power counterbalancing that of Japan (Orme, 1996). Hence the extent of centralized policy coordination within the region is low, and ASEAN has developed a very open institutional character.

5.3.3 Southern African Development Community (SADC)

The Southern African Development Community (SADC) establishes trade relations among twelve nations in Sub-Saharan Africa: Angola, Botswana, the Democratic Republic of Congo, Lesotho, Malawi, Mauritius, Mozambique, Namibia, the Seychelles, South Africa, Swaziland, Tanzania, Zambia and Zimbabwe. SADC was formed in 1992 on the foundations laid by the Southern African Development Coordination Conference (SADCC) in 1980. Whereas the SADCC had no legal identity, SADC is institutionalized by treaty, although the treaty calls for a rather limited scope for cooperation.
The region is dominated by South Africa, whose GDP at the time of the RIA's formation was 75 percent of the regional total. As a consequence, South Africa has a tendency not to consult other member countries on trade arrangements with far-reaching consequences, such as commitments to WTO requirements, unilateral trade liberalizations and subsequent indirect market penetration by foreign firms, and negotiations with the EU on bi-regional free trade (Ten Napel, 1998). The latter, for instance, would threaten the privileged access

to the European market which many other SADC members enjoy under the Lomé Convention (preferential access for former colonies).
SADC was never intended as an ISI or autarkic growth program, but rather a form of 'defensible multilateralism'. Trade relations are unbalanced, with South Africa being relatively unilateral in its aggressive penetration of other African markets (Ten Napel, 1998). As a development paradigm this could be designated a 'flying geese' scenario (Boudhan, 1997) or from a trickle-down perspective as a potential regional growth hub. In terms of bargaining power and dependency, the trade imbalance is better described as a core-periphery relationship that solidifies the hegemonic position of South Africa.
To the extent that the SADC has generated increased economic activity, the role of South Africa and improved trade relations after the end of Apartheid regime were instrumental. Hard to say if all trade activity prior to 1991 was accurately reported. clear that the SADC is largely externally oriented in its trade relations, much as other developing country initiatives (see Mercosur and ASEAN above). This is in part a reflection of the member countries' colonial past. In addition the trends reflect the general liberalization undertaken under IMF auspices among many African countries around 1990.

5.3.4 Trends in trade activity and openness: Mercosur, ASEAN and SADC

In ASEAN, the trend towards increased decentralization of Japanese control may explain the shift in activity (i.e., formal 'ownership' of sales and assets implies direct control) from Japan to Asia between 1993 and 1997. Networks of indirect, structural control over large parts of the Asia region could complement the networks of indirect, structural control in Japan. In particular ASEAN became strongly influenced by Japan, thus creating a semi-periphery in a comparable manner as Central Europe for the European Union. However, with one big difference: Central Europe became part of the production network of the European Union as an extension of the macro-Fordist concept of control, which contains substantial formal integration. ASEAN became part of the Toyotist production networks, which implies preferably informal (and thus shallower) integration, but highly outward in orientation. Mercosur revolves largely around the cautious distrust between its two largest members, Argentina and Brazil, and can be seen as an attempt to lock their respective economies together in such a way that trade economics are less easily used as a weapon in that distrust. SADC centers on the position of South Africa as hegemon, which is to lead the drive for trade growth and development from the inside out.
Analysis of their relative openness is limited here to trade data due to the limited availability and unreliability of FDI data at the country-to-country level for these countries. The trade data show mixed base values that reflect the divergent strategic realities and divergent migrations (Table 5.5). Mercosur countries, which began with a relatively low level of trade, were actually trading more *before* the introduction of the RIA, with the trade to GDP ratio dropping from 12 percent in 1984 to seven percent in 1991. Although this trade level remained essentially unchanged over the subsequent decade, trade became considerably more inward-oriented, with the ratio of extra- to intra-regional exports dropping from around 12:1 in the period 1984-1991 to around 4:1 in 1991-2001.
ASEAN and SADC had similar trade-to-GDP ratios in the 1980s that paralleled that of world trade (ca. 24 percent), but while that ratio declined for SADC as a whole over the 1990s, for ASEAN it exploded to as high as 75 percent in 2000. At the same time ASEAN was able to maintain a general outward orientation, dropping only slightly from over 4:1 to

over 3:1 in the course of the 1990s. SADC, on the other hand, has grown increasingly inward oriented. After having been the most outwardly oriented of all regions, with an extra- to intra-regional trade ratio of 25 percent, it has become less and less so, ending the decade just twice as outwardly oriented as ASEAN or Mercosur.

Table 5.5: Trade trends: Mercosur, ASEAN and SADC, 1984-2001

	Mercosur		*ASEAN*		*SADC*		*World*
Year	% of GDP	E/I	% of GDP	E/I	% of GDP	E/I	% of GDP
1984	12.2%	14.90	26.2%	4.30	24.0%	24.57	23.0%
1985	11.0%	17.05	30.3%	4.37	26.6%	26.37	22.4%
1986	7.9%	10.77	29.3%	4.99	25.7%	25.09	21.1%
1987	8.2%	12.09	32.8%	4.67	26.8%	25.99	21.8%
1988	9.6%	13.94	37.6%	4.68	23.0%	23.90	22.6%
1989	8.7%	11.56	41.0%	4.55	23.3%	28.24	23.3%
1990	7.3%	10.43	41.9%	4.25	22.8%	22.04	23.3%
1991	7.8%	8.00	43.7%	4.04	20.5%	14.43	23.0%
1992	8.1%	5.98	43.9%	4.06	19.9%	12.43	22.9%
1993	7.6%	4.36	44.5%	3.75	20.3%	12.06	23.2%
1994	7.2%	4.14	47.7%	3.31	20.8%	10.28	24.7%
1995	7.1%	3.96	50.0%	3.19	21.2%	7.82	27.1%
1996	7.0%	3.40	47.7%	3.16	23.4%	7.61	27.2%
1997	7.2%	2.98	51.8%	3.34	20.9%	10.66	27.9%
1998	7.2%	2.81	69.9%	4.46	21.0%	7.68	27.0%
1999	7.0%	3.87	66.5%	3.55	21.2%	8.10	27.2%
2000	9.5%	3.79	75.3%	3.21	20.0%	7.00	29.6%
2001	10.0%	4.19	69.9%	3.40	20.0%	8.24	28.1%

5.4 Understanding regionalism in a multilateral system

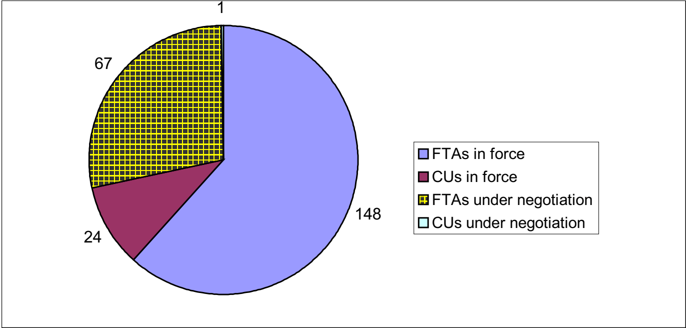
In order to draw conclusions on the place of regionalism in the broader global system, several of the tools and concepts explored in the preceding sections as well as Chapter 3 can be applied. First, some observations will be made based on the dominant forms and composition of RIAs in the world today in terms of their general characteristics. Second, policy-level strategies will be positioned in the 'multilateral-regional-unilateral' framework introduced in Chapter 3 to demonstrate how the choices countries make can be understood in relative terms. Third, the role of trade disputes within the WTO will be discussed to shed light on regionalism within these positioning strategies. Lastly, the outcomes of integration across the five RIAs will be analyzed on the basis of the macro evidence, discussing the 'strategic migrations' evidenced by trends in trade and investment.

5.4.1 Type and composition of the world's RIAs

The WTO, in contrast to the diverse characterizations of more theoretical approaches, applies the distinction between Free Trade Areas (FTAs) and Customs Unions (CUs) in differentiating between RIAs with a common external tariff and those without. From the WTO's perspective, FTAs are more attractive given that CUs have a higher potential for

protectionism behind the CET. According to the WTO, the bulk of the 240 RIAs notified to the WTO as of July 2000 (both those in force and those under negotiation) are FTAs and therefore suggest a more open global trade environment (Figure 5.2).

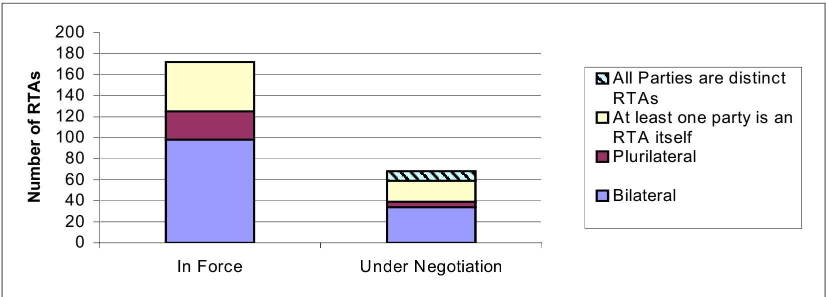
Figure 5.2: RTAs in force and under negotiation as of July 2000, by type of RTA



Source: WTO

Additionally, the WTO points to the increased tendency of existing RIAs to become themselves party to new RIAs (Figure 5.3). Most RIAs under the WTO definition are bilateral, or between two countries (accounting for almost 60 per cent of the 172 RTAs in force, and for half of all RTAs under negotiation: WTO, 2000). Plurilateral RIAs, such as those under consideration in the current study, account for only 16 per cent of all RIAs currently in force, but make up less than ten per cent of RIAs under negotiation. This suggests that the 'second wave of regionalism', to the extent it can be characterized as a plurilateral phenomenon, may have crested and is likely waning.

Figure 5.3: Composition of RTAs



Source: WTO

The percentage of RIAs where at least one party is an RIA itself is about 30 per cent (e.g. the EU, EFTA, Caricom and CACM). The WTO expects RIAs of this type to increase in the future (e.g. EC-MERCOSUR and Closer Economic Relations (CER)-Association of South East Asian Nations (ASEAN). These account for nine of the 68 RTAs under negotiation and are composed of both regional and cross-regional initiatives. This is a new

trend which reflects the growing consolidation of established regional trading arrangements (WTO, 2000).

5.4.2 The WTO as a forum for multilateralism and regionalism

The primarily economics-centric debate on globalization and regionalization has a political counterpart in the debate between multilateralism and regionalism. As argued in Chapter 3 (section 3.4), countries have various options for positioning in the global order, assuming at the two extremes either a multilateralist stance or a unilateralist stance, or more moderate strategies of unilateral regionalism or parallel regionalism-multilateralism. An analysis of WTO trade dispute activity can provide insight into the relative importance countries attach to the multilateral system. As of December 5, 2002, a total of 273 consultations had been requested via the WTO since January 1, 1995. A number of those consultations were initiated by multiple parties, raising the number of complainants before the WTO to 303. Ten parties account for more than three-quarters of all the complaints raised before the WTO (Table 5.6). The US alone accounts for one quarter. The EC of course represents 15 countries, but has a fairly harmonious and unified trade policy in which the European Commission speaks on its members' behalf.

Table 5.6: Origins of trade disputes before WTO, 1995-2002

complainant	*1995*	*1996*	*1997*	*1998*	*1999*	*2000*	*2001*	*2002*	*Totals*	*% of total*
US	6	17	17	10	10	8	1	3	72	23.8%
EC	2	7	15	16	7	7	2	3	59	19.5%
Canada	5	3	1	4	2	1	3	3	22	7.3%
Brazil	1	0	3	2	0	3	7	5	21	6.9%
India	1	4	0	3	1	1	3	2	15	5.0%
Japan	1	3	1	1	2	0	1	2	11	3.6%
Mexico	1	4	0	0	3	1	1	0	10	3.3%
Chile	1	0	1	0	0	0	4	2	8	2.6%
Thailand	1	3	0	0	1	1	2	0	8	2.6%
Argentina	0	1	0	1	0	1	1	3	7	2.3%
Other	6	12	8	7	9	7	11	9	70	22.8%
Totals	**25**	**54**	**46**	**44**	**35**	**30**	**36**	**33**	**303**	

Note: Total number of complainants (303) is greater than the total number of disputes (273) due to a small number of cases in which multiple parties are complainant

Four major RIAs are represented in the 'Trade Dispute Top 10': the NAFTA, EU, Mercosur and ASEAN. In the case of NAFTA, all three member countries are in the list. The EU is represented by the EC, and Mercosur's two main countries (Brazil and Argentina) as well. Thailand tops the list representing ASEAN. Additionally, two go-it-aloners (Japan and India). In addition to the Top Ten, 26 additional parties have pursued dispute settlement one or more times before the WTO. African countries are absent in the entire list. In order to relate regionalism to multilateralism, however, WTO DSP activity must be considered in relation to the RIA to which parties are members. Some RIAs provide for dispute settlement procedures (DSPs) at the regional level, others do not. NAFTA, for instance, has DSPs that allow for deferral to the WTO, and in that sense it is not surprising that NAFTA countries, with the US at the fore, are the primary complainants at the WTO, accounting for over one-third of the total (Table 5.7).

Table 5.7: Intra- vs. extra-regional trade disputes before WTO, 1995-2002

	NAFTA	*EU*	*Mercosur*	*ASEAN*	*SADC*	*Other*	*Total*	*Intra/extra*
NAFTA	19	37	10	4	0	34	104	18.3%
EU	29	0	12	1	0	17	59	0.0%
Mercosur	14	8	2	0	0	6	30	6.7%
ASEAN	5	2	2	1	0	6	16	12.5%
SADC	0	0	0	0	0	0	0	n.a.
Other	37	18	9	4	1	25	94	
Total	104	65	35	10	1	88	**303**	

Hence, nearly 20 percent of total NAFTA are consultations requested from other NAFTA countries (intra-regional disputes). Even though WTO activity by NAFTA countries is in the procedural sense not surprising, it remains remarkable that regional members would have so many disputes with other regional members at all. This activity has waned considerably since 1999 however. Still, it suggests that either the NAFTA does not address all the issues of major concern to its members, or that NAFTA members did not have enough of a common vision or motive in entering into the agreement.

Members of the EU, on the other hand, have never lodged a complaint against fellow EU member countries. Mercosur is home to the third-largest group of complainants, accounting for 12.5 percent of the cases presented. Of the cases raised, just over 15 percent were directed at fellow Mercosur countries. A unique case is the CEFTA; although only 7 members were involved in consultation requests during the period, most (5) were directed at other CEFTA members.

Interestingly, in most cases complaints between regions or regional members are more or less in balance. While NAFTA countries have lodged complaints 104 times, they have also had 104 complaints lodged against them. The EC has requested consultations 59 times, either on its own or on behalf of a member state, and has been subject to a consultation request 65 times. Mercosur countries have complained 38 times, and been targeted 37 times. Even more striking is that *inter*-regional disputes also tend to be balanced. A noticeable exception is the EU and NAFTA. The EC has requested consultations 29 times with NAFTA member countries, while NAFTA members have lodged complaints 37 times against the EC or one of its members. Only 94 of the 303 complainants (30 percent) were not members of any of the five RIAs in question. Of these, three countries (Japan, India and South Korea) accounted for nearly a third.

5.4.3 Opting out and 'going it alone'

Some larger countries have chosen to stay out of the second wave of regionalism. The most noticeable cases are Japan and South Korea, India, China and Russia (or the Russian Federation). Applying the same technique of analysis to these five countries, the following observations on their openness and/or closedness in trade and investment can be construed. On the whole the 1990s showed an increased openness towards trade, which could imply that the growth of real world trade has been primarily linked to the countries that did not engage in RIAs. The picture for the five countries is mixed, however (Table 5.8).

Table 5.8: Going it alone: Exports and imports as percentage of GDP, 1980-98

	India		*Japan*		*China*		***South** Korea**		*Russ. **Fed.*****	
	Export	Import	Export	Import	Export	Import	Export	Import	Export	Import
1980-84	6.4	9.2	14.4	13.4	7.9	7.4	35.1	38.2	-	-
1985-89	6.5	9.3	11.4	8.5	12.1	13.8	36.6	31.5	-	-
1990	7.7	10.6	10.7	10.0	14.8	12.1	29.8	30.3	18.2	17.9
1991	9.3	9.9	10.2	8.5	16.2	13.4	28.6	30.6	13.3	13.0
1992	9.7	11.0	10.1	7.8	16.3	15.3	28.9	29.9	55.6	50.5
1993	10.8	12.2	9.3	7.0	14.4	16.4	29.3	28.8	35.5	31.6
1994	10.8	13.5	9.3	7.2	21.9	20.6	30.1	30.8	27.7	22.9
1995	11.9	15.3	9.4	7.9	21.0	19.3	33.1	34.1	26.4	22.7
1996	11.6	15.5	9.9	9.4	21.0	18.9	32.4	36.3	24.1	20.1
1997	11.6	15.5	8.8	-	23.0	18.5	38.1	38.8	22.9	20.2
1998	11.0	14.0	8.3	9.6	19.1	14.3	48.7	35.8	31.7	26.7

Source: World Bank Development Indicators and Country Reports 1999, and OECD Statistical Compendium

** decrease 97-98 of GDP 33%*

*** decrease 97-98 of GDP 14%*

Since 1984, Japan has experienced a constant decrease of its relative exports and imports. In the first place this position was enhanced by deteriorating exchange conditions due to the Plaza Agreement. In the second place were exports substituted for by direct production in the most important markets and the consequent international investments of Japanese companies (see below). International production for most Japanese multinationals contained very low profitability margins (See the Templeton Global Performance Index, 2000) which created additional barriers for increased exports.

India's exports over the 1980s stabilized (often in the form of counter-trade) at a low level. When a growth spurt appeared in the 1988-1993 period, this was relatively short-lived and modest. At the same time imports only slightly increased, and since 1995 again started to decrease as a percentage of GDP. Compared to the other developing countries, India therefore has remained the most closed economy in practice, notwithstanding major liberalization initiatives in the course of the 1990s.

South Korea's industrialization model has been built upon exports. The country has become increasingly open towards exports, whereas the share of imports in GDP declined since the 1980s. South Korea experienced lower exports in the 1990s in comparison with the 1980s. It could be hypothesized that - like Japan - South Korea suffered from its position outside of the most important markets, while a reorientation towards markets in developing regions had to be accompanied also by local production and thus had an equally negative effect on its export performance. At the end of the 1990s South-Korea experienced a period of quick relative export growth, but this appeared only because of a tremendous decrease in the national GDP as a consequence of the Asia crisis.

China started its go-it-alone strategy from the most closed position of all countries under consideration. At the end of 2000, the country has not yet become member of the WTO, but export growth has increased with leaps and bounces, probably closely linked to timely changes in trade regime. But, since 1994, the trade position of China has become more closed with stagnant exports (as percent of GDP) and declining imports. At the same time inward FDI increased tremendously (see below) hinting at a substitution of imports and exports by direct production in China.

The trade picture for the Russian Federation has been rather volatile. Throughout the period the country has still experienced some openness in trade with around twenty percent of GDP dedicated to exports and imports. The Russian trade environment presents in any case a rather unstable surrounding for firms to operate in.
The above analysis suggests that becoming voluntarily detached from the world economy – like China and the Russian Federation or India – has been accompanied by growing exports, whereas the more or less involuntary isolation of in particular Japan has lead to decreasing exports and to low relative levels of embeddedness in the world trade system.
Go-it-alone strategies are best operationalized in countries' investment regimes. Table 5.9 considers the trends in inward and outward investment for the five countries over the 1980-1997 period.

Table 5.9: Going it alone: inward and outward FDI stocks as a percentage of GDP, 1980-97

	India		Japan		China		South Korea		Russian Federation	
	In	Out	In	Out	In	Out	In	Out	In	Out
1980	0.7	0.1	0.3	1.9	-	-	1.8	0.2	-	-
1985	0.5	0.1	0.4	3.3	1.5	-	2.3	0.5	-	-
1990	0.4	-	0.3	6.9	5.2	0.7	2.3	0.9	-	-
1995	1.6	0.2	0.7	4.7	18.8	2.3	2.3	2.2	1.6	0.9
1997	3.3	0.3	0.6	6.5	23.5	2.2	3.3	0.3	3.2	1.4

Source: UNCTAD, 1999

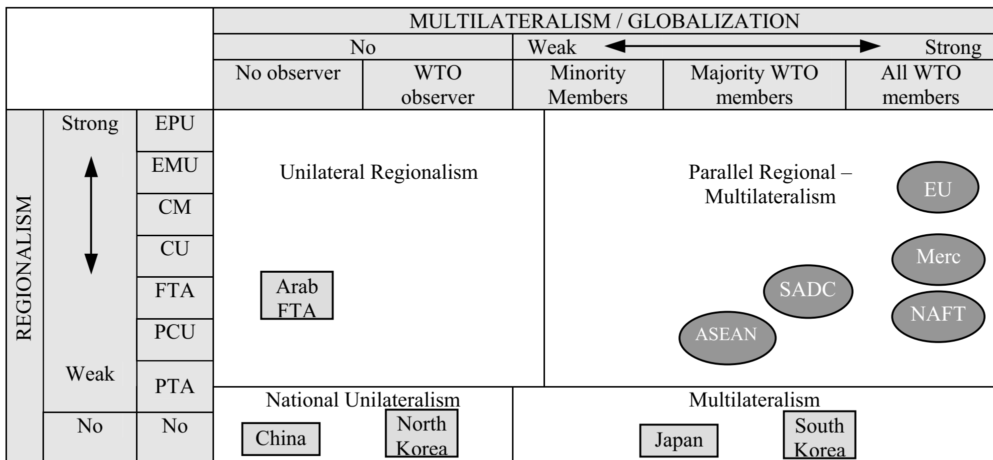
In absolute terms, all five countries are relatively closed towards inward as well as outward FDI stock. The only exception has become China that has been the prime target country for inward FDI in the 1990s due to a policy of controlled opening up to FDI. Hardly anybody would dispute that China's investment regime is still considerably more closed than the investment regimes of most other countries.
Over the 1980-1997 period all developing countries have experienced increases in inward FDI: India and Russian Federation modest increases, China major increases. The Chinese development model therefore is much more focused on development aided by FDI. India and the Russian Federation remain the most closed countries in investment terms.
The two developed countries of this grouping have amongst the lowest inward FDI as compared to any of the countries in the RIAs discussed above. Compared to India and the Russian Federation they or at least as closed, taking inward and outward FDI flows into consideration. Both countries have hardly subscribed to bilateral investment treaties with other OECD countries, creating major risks for companies investing in these countries, which has resulted in stagnant or even negative flows of inward FDI. For Japan inward FDI stagnated at very low levels in the 1980-1990 period and further declined since 1995. For South-Korea inward FDI stagnated in the 1985-1995 period. Stagnation in inward FDI thus appeared in the period in which both countries inaugurated their economic 'jump forward', which got accompanied by an increase in outward FDI.
Firms from the same two countries also engaged in retreat strategy at various periods. Japanese firms already declined their outward FDI in the early 1990s as the effect of the formalization of NAFTA and EU (and the lingering fears of fortresses in North-America and Europe), and the slow deflation of the domestic bubble economy. South-Korean firms started to retreat to their domestic economies in the second half of the 1990s as the

consequence of the 1997 Asia Currency crisis, pointing at the relative weak position of the economy. For both countries their retreat strategies represents the desire to recuperate when in crisis by creating a more closed system which is easier to restructure than a more open system. Both countries have also been fairly passive in supporting RIAs in the Asia region. Note that Japan and India are both WTO members and listed in Table 5.6 as frequent users of WTO DSPs. Therefore opting out of regionalism in some cases reflects a preference for multilateral channels and in others a true 'unilateralist' stance.

5.4.4 Three 'isms' in practice: multilateralism, regionalism and unilateralism

In Chapter 3 a conceptual framework of possible combinations of multilateral, unilateral and regional strategies was presented. The strength of multilateral, unilateral and regional tendencies can be operationalized at the political level in terms of country membership in regional and / or multilateral organizations. The horizontal axis shows how intensive participation is in the quintessential (trade- and investment-related) international organization, the WTO. A country or group of countries can either be all full WTO members, or a majority or minority of the group. Some countries, however, only have observer status or none at all. At the same time a country the strength of a country's regionalist tendencies can be approximated by the intensity, depth or strength of the RIA. An EPU, for example, demonstrates a greater commitment to regionalism than a PTA. Figure 5.4 provides an indication of how the five RIAs under consideration can be placed along these two axes, along with a number illustrative examples of other strategies.

Figure 5.4: Positioning RIAs in the globalization debate



The five RIAs under review can all be considered examples of parallel regional-multilateralism. The EU, Mercosur and the NAFTA all comprise exclusively WTO members but vary in the strength of their regionalism. In the case of the SADC, one country is not a member of the WTO (Democratic Republic of Congo) and therefore is an example of a slightly weaker parallel regionalism-multilateralism strategy. ASEAN is the

weakest example of parallel regional-multilateralism, since it is only a weak FTA and only seven of its ten member countries are full WTO members. By contrast, Somalia, Syria and Iraq form part of the Arab Free Trade Area yet are not members of the WTO. This can be characterized as a unilateral regionalism strategy. Countries like China (until 2002) and North Korea can be qualified as unilateralist, while Japan and South Korea pursue exclusively multilateralist strategies.

5.4.5 Migratory strategies: shifts in RIA openness over the 1990s

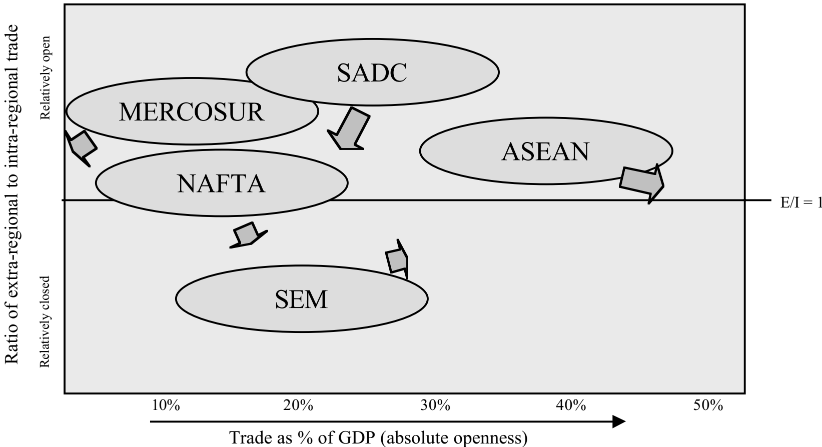
Table 5.10 below summarizes the trade and FDI data analyzed for the individual RIAs discussed above. It provides average values of the key indicators over the 5 years preceding implementation of the RIA (the 'pivot year') and the 5 years following. The pivot year itself is not included in the averages.

Table 5.10: Summary of trade and FDI data for key RIAs

		Trade/GDP		*Extra/Intra*		*FDI/GDP*		*Extra/Intra*	
Region	Pivot year	5 yr pre	5 yr post	5 yr pre	5 yr post	5 yr pre	5 yr post	5 yr pre	5 yr post
EU	1992	22.4%	23.4%	0.54	0.62	12.27%	16.52%	1.42	1.00
NAFTA	1994	8.8%	11.1%	1.35	1.03	8.4%	12.0%	2.86	3.51
ASEAN	1992	39.4%	48.3%	4.44	3.35				
SADC	1992	23.3%	21.3%	22.92	9.68				
Mercosur	1991	8.3%	7.4%	11.76	4.37				

Figure 5.5 visualizes the migrations described in Table 5.10.

Figure 5.5: 'Migration' in levels of openness, pre- versus post-RIA implementation



NAFTA and the European Union are the only regions in the world in which intra-regional trade prevails over extra-regional trade. The figure also shows how the EU, although relatively closed in terms of it outward orientation and average in terms of the importance of trade to the economy, has been moving up and to the right, and therefore is slowly but

steadily becoming increasingly open. The NAFTA and Mercosur, while departing from more or less the same position, are diverging in terms of the importance of trade to the economy while both turning relatively inward in orientation. The SADC is heading in the general direction of Mercosur and to a lesser extent the NAFTA, becoming increasingly closed both relatively and absolutely.

It should be noted that the in terms of FDI, developments over the horizontal axis for the two regions considered are more or less identical to those in trade, yet over the vertical axis both the NAFTA and the EU show contradictory trends. The NAFTA is becoming increasingly inward looking in terms of trade, but increasingly outward in terms of investment. In addition, FDI is more important relatively than trade. The EU, on the other hand, is trading more extra-regionally but investing more within the home region.

5.5 Macro-level conclusions

Despite the iron-clad logic of traditional trade theory, real-world trade treaties 'cannot prohibit rude surprises' (Orme, 1996: xix). The devil of a trade arrangement is in the details: the tariff reduction schemes, the phase-outs, and the opt-out industries. It's hard to say if increasing 'closedness' in developing regions is negative or positive. In strict terms it signifies a retreat in globalization, but only in relative terms. The absolute value of trade from and to these regions has grown; intra-regional growth has simply been higher. This may signify increasingly regionally-constructed divisions of labor.

In Chapter 3 and the preceding analysis, we have made observations about the form of integration, the depth of integration, the underlying motives, the key policy instruments implemented, the economic and political power balance among the member nations, the development factor, economic logic and assumptions of firm behavior, and the nature of government-business relations in and between the member countries. An overview of the conclusions is given below in Table 5.11.

Table 5.11: Overview of main characteristics of key RIAs

	SEM	***NAFTA***	***Mercosur***	***ASEAN***	***SADC***
Form of integration	Common Market	Free Trade Area	Customs Union	Preferential Trade Agreement	Free Trade Area
Dynamism over 1990s	Depth: ⇒ MU; Enlargement: high	Depth: Static Enlargement: high (FTAA)	Depth: Static Enlargement: low	Depth: ⇒ FTA Enlargement: low	Stagnating due to lack of growth and synergy
Primary policy instrument(s)	Internal tariff and NTB reduction	Rules of origin (local content rules)	Common External Tariff	Ministerial meetings, intended FTA	Preferential market access
Explicit rationale / motives	Collective action problem: coupling regional supply and demand	US: enhancement of national power Mexico: lock-in	Growth through scale (large market)	Initially security-related	Export-led growth; defensible multilateralism
Economic asymmetry	Developed economies	Developed - Developing	Developing	Developing	Developing
Political asymmetry	Pluralist 'core axis'	Internal hegemony (US)	Dual hegemony (Braz. / Arg.)	External hegemony (Japan)	Internal hegemony (South Africa)
Within multilateral system	Parallel regionalism - multilateralism	Parallel but moving towards unilateralism	Multilateralism *through* regionalism	Primarily multilateralism	Unilateral regionalism

6. INTERNATIONALIZATION AT 'T-MINUS': BASELINE 1990

In relation to the policy-level vision of structural change, 'the reality of integration is likely to be less tidy' (Wartick and Wood 1998: 50) due to the myriad complexities in barriers to and patterns in trade and investment. Although the policy mechanisms used on the basis of the policy-level strategic intent combine to determine the policy level outcome, realized restructuring is conducted by firms, with core companies at the fore. Since regionalism strategies may differ between firms and governments, the latter in particular run the risk of basing their choices on oversimplified notions of firm behavior. The macro-data reviewed in Chapter 5 created a backdrop for positioning various regionalism strategies within the broader multilateral context, but from that data very limited inferences can be drawn as to the behavior of firms.

How did core companies internationalize and restructure over the 1990s, and was there a clear difference between the period prior to regional consolidation (1995) and the period afterwards? Before embarking on a longitudinal exploration in pursuit of 'regionalism effects', it is necessary to provide a 'static' picture of the positioning, internationalization and control strategies core companies pursued prior to the second wave of regionalism. For this purpose 1990 has been chosen as the 'baseline'; the post-1990 dynamics will be investigated in Chapter 7. Additionally, many of the empirical constructs are new and as such require adequate attention before being analyzed over time.

The first step in the firm-level empirical investigation is to select a sample of core companies for analysis (6.1). These companies will then be categorized in terms of their horizontal and vertical positioning strategies (6.2). Section 6.3 explores various measures of internationalization for the set, and section 6.4 addresses core company network structures and control strategies. These analyses will be brought together in Section 6.5 to 'typologize' the sample according to the strategy framework laid out in Chapter 4.

6.1 Sample selection

Companies as micro actors in regional integration refer to companies, multinational or not, which are not only directly affected by regional integration, but also have a stake in shaping the outcome. In practice this amounts to companies with sufficient geographic scope and financial resources to enact restructuring on a regional level, as well as the bargaining power to influence national and/or regional policy stances. Such companies can also be indicative of industry-wide trends because their restructuring has ripple effects through the rest of the value chain (Lall, 1980). Attempts to explore the power base of companies such as the 'flagship firms' of D'Cruz and Rugman (1997) and 'leader firms' of Baden-Fuller and Lorenzoni (1995) are often based on intuitive identification or on a single indicator. These characterizations tend to miss more subtle aspects of company power such as technological advantage, political involvement or horizontal / vertical positioning.

6.1.1 The SCOPE database: a selection of core companies

The SCOPE database, initiated in 1997 at the Studies and Competence center for Organizational and Policy research in European Business (SCOPE) at the Erasmus University of Rotterdam, addresses many of these conceptual and methodological gaps and

forms the basis for the current study. The SCOPE database documents financial and strategic information of the 200 world's largest (non-financial) companies over the 1990s (the Core200), selected by value of total sales in US dollars in 1995 (see Van Tulder *et al*., 2001). The SCOPE database monitors a predetermined sample of large firms over a longer period of time, instead of selecting a sample each year, such as the Fortune 500 or the UNCTAD Top 100 TNCs.
SCOPE provides information on the geographic spread of assets, sales, employment, and affiliates of the Core200 from 1990 to the present, in addition to various other aspects of core company activity such as R&D expenditure, historical development and corporate social responsibility (CSR) strategies. Some of this output is published annually in UNCTAD's World Investment Report. Data are collected from annual reports, company surveys, interviews and secondary public sources (see also Appendices II and III). The database is intended to function as a tool for research at the Erasmus University as well as collaborative efforts with partner universities, based on a shared theoretical view of the importance of core companies in national, regional and global economy.
Although size is an initial (but by no means exhaustive) criterion, SCOPE explores numerous additional dimensions of core positioning and strategy, such as technological strength (R&D expenditures, patent registration), links between core companies and governments (e.g. public offices of company CEOs and board membership of heads of state), and core company positioning strategies (e.g. the distinction between core power based on extensive vertical control over industries and core power based on a horizontal 'choke-hold' on distribution). Additionally, the SCOPE database is highly international in composition, representing companies from 15 countries (see table 6.1).

Table 6.1: Core companies per country of incorporation in SCOPE Core200

Country of origin	*# of companies in Core200*	*Country of origin*	*# of companies in Core200*
Brazil	1	Spain	3
Canada	1	Sweden	3
France	20	Switzerland	2
Germany	23	Switz./Sweden	1
Italy	5	United Kingdom	7
Japan	60	UK/Netherlands	2
Mexico	1	United States	61
Netherlands	3	Venezuela	1
South Korea	6		
	Total		**200**

The Core200 is a diverse group of companies from many countries, involved in many activities. Since the objective of the research is to study the (diversity in) strategic responses to regionalism among core companies, the sample studied should be representative of core companies in general (or even relatively exhaustive) instead of choosing e.g. a sector, or country. Therefore the sample should be broad in order to reflect those nuances, as opposed to a narrow focus which *over*emphasizes the role of institutional factors in strategy. Cross-sectional research of this nature, first made popular by Bain (1956), can produce useful analysis (Ghemawat, 1994). According to Schmalensee (1989:

952), cross-section studies 'rarely if ever yield consistent estimates of structural parameters, but they can produce useful stylized facts to guide theory construction…'.

The aim of the current study is more one of 'stylized facts' than of 'structural parameters'. Most of the objections Schmalensee addresses arise in large part from the desire to establish observable equilibria in the economic sense. Since this study is aimed less at statistically rigorous parameters and more at producing a general picture of organizational responses by a diverse sample of firms to regional integration, cross-section analysis may be very useful. Additionally, core companies themselves usually span multiple sectors in the traditional sense, such that firm level data are thus 'multi-market aggregates' (Schmalensee, 1989: 962). This point will be taken up in the following section.

More generally it can be argued that success among core firms is not only measured by success relative to the arbitrary 'sector' competitor, but in the sense of higher growth and profitability than other (core) companies in general. In other words, total global demand is finite, and there is a certain amount of inter-sectoral competition for that finite demand; in other words, there is competition for consumer 'dollars' across sectoral boundaries. Many goods are substitutes even though they do not address the same utility. The choice to buy a new car and the choice to buy a new refrigerator, for instance, can be interdependent, even though a strictly sectoral approach would not consider Whirlpool and Ford to be competitors.

In order to increase the focus in the sample, maintain the manageability of the study in general and at the same time maximize the likelihood of identifying various 'regional integration effects', the study addresses only firms based in the two regions under consideration. Policy studies aim particularly at insider companies; therefore the selection is of core companies from the SCOPE Core200 based in SEM and NAFTA member countries. In addition, Swiss core companies were included on the grounds that a firm's country of incorporation may theoretically not be directly related to a company's strategic reality, if it for example has sufficient intra-regional activity to have a clear vested stake, and are thus comparable from a policy-mechanism standpoint to 'insider' firms.

Based on these considerations, a list of 122 core companies emerged as a potential sample for analysis. Firstly, US, Canadian and European (EU15) core companies were selected (128) based on criterion 1. The two Swiss firms and the joint Swiss-Swedish firm were included on the basis of criterion 2. Nine companies, mostly state-owned and / or domestic, had to be dropped due to a lack of data availability (Deutsche Bahn, Deutsche Post, Deutsche Telekom, Teneo, Repsol, La Poste, US Postal Service, United Parcel Service). Table 6.2 lists the final 122 candidates for the study.

Compared to the total number of firms operating in the world, 122 is a small sample size. But of the world's core companies, these 122 the largest, most politically active and economically powerful. Together they had a combined asset value in 1990 of $US *3.2 trillion*. Note that since the benchmark year 1990, a number of the companies listed in Table 6.2 have merged, been acquired, or undergone name change that otherwise alter the character of the sample. These changes do not automatically disqualify the companies in question; rather, they constitute to some degree at least one aspect of the strategies pursued by those companies during the period. These changes will be taken into consideration in the longitudinal analysis as they arise.

Table 6.2: Core companies in the sample

Core companies, alphabetically			
3M	Digital Equipment	IRI	Rhone Poulenc
ABB	Dow	J C Penney	Robert Bosch
Ahold	Du Pont	J Sainsbury	Royal Dutch Shell
Albertson's	EDF	Johnson & Johnson	RWE
Alcatel	Electrolux	Karstadtquelle	Safeway
AlliedSignal	Elf Aquitaine	Kmart	Saint-Gobain
Amoco	Enel	Kodak	Sara Lee
AMR	ENI	Kroger	Sears Roebuck
ARCO	Ericsson	Lockheed Martin	Siemens
AT&T	Exxon	Lufthansa	Suez
BASF	Federated Dept Stores	Mannesmann	Supervalu
BAT	Ferruzzi	Marathon Oil	Target
Bayer	Fiat	McDonnell Douglas	Telefonica
BCE	Fleming	Merck	Tesco
BellSouth	Ford	Metro	Texaco
BMW	France Telecom	Mobil	Thomson
Boeing	Franz Haniel	Motorola	Thyssen
Bouygues	Fried. Krupp	Nabisco	Total Fina
BP	Gen. des Eaux	Nestlé	UAL
BT	General Electric	Novartis	Unilever
BTR	General Motors	Pechiney	United Technologies
Carrefour	Georgia-Pacific	Pepsico	Usinor
Caterpillar	GTE	Peugeot	Veba
Chevron	HCA	Philip Morris	Viag
Chrysler	Hoechst	Philips	Volkswagen
Coca-Cola	Home Depot	Pinault-Printemps-Redoute	Volvo
Compaq	HP	Preussag	Wal-Mart
Conagra	IBM	Procter & Gamble	Worldcom
Costco	ICI	Promodes	Xerox
Daimler-Benz	Intel	Rag	
Danone	International Paper	Renault	

6.1.2 National origins

Table 6.3 shows the breakdown by home country (country of incorporation). Of the 122 companies, 55 percent are based in Europe and another 45 percent are based in North America (all but one in the US). As a subset of companies in general, the sample is fairly small. As core companies, however, the sample is representative for the overall core company population in the two regions. In that sense ‘200’ is a relatively arbitrary cutoff point since there are of course other firms that may function as core companies but fall outside the scope of the study. Yet the measurement indicators of core status – size in particular– decline dramatically below that point. The largest core company measured by total assets in 1990 (General Motors) was more than 500 times larger than the smallest

(HCA/Healthcare). The composition of the sample also means that biases such as country of affiliation and sector will be reflected in the analysis. There will, however, be no attempt to 'correct' for these biases, but rather to emphasize their significance and relevance for the analysis. Just as some countries are larger and more influential in macro-level processes, some countries also have more core companies, and different core companies, than their neighbors. These differences are an active ingredient in the strategic game at both levels.

Table 6.3: Sample characteristics by country of incorporation

Country of origin	*# of companies in sample*	*# of companies in SCOPE Core200*	*Avg asset value, 1990 ($US mil)*
France	19	20	$24.156
Germany	20	23	$18.040
Italy	5	5	$55.495
Netherlands	2	3	$16.529
Spain	1	3	$33.916
Sweden	3	3	$12.581
Switzerland	2	2	$30.247
Switz./Sweden	1	1	$21.008
United Kingdom	7	7	$23.753
UK/Netherlands	2	2	$59.847
United States	59	61	$27.168
Canada	1	1	$32.348
Total	**122**	**131**	**$26.192**

Home country matters because of the embeddedness a core company has in its historical environment. Its core networks are constructed largely on the basis of the home bargaining environment, and network elements outside the home country are conditioned based on the strategies developed historically within the home country. Once a business is established, it is locked in through learning, circular causation and cumulative causation effects that tie it to its home country (Jovanovic, 2001). Some argue that core companies share more interests with each other than they do with their respective national governments (Vernon, 1998), but as argued in Chapter 4, concepts of control are to some extent nationally determined. Both the bargaining environment and the 'lock-in' effects of e.g. learning and culture suggest that country of origin will also be a determinant in internationalization strategy in general (KPMG, 2000; Hirst and Thompson, 1999; UNCTAD 1998, 1999) as well as under regional integration in particular (Davies *et al*., 1999; SMR 1997).

The countries of origin in Table 6.3 are of different sizes (GDP) and with varying representation among the sample. Statistical analysis with diversity of this kind is difficult and its outcomes unreliable. While an *N* of more than five per country is a prerequisite for even the most tentative non-parametric tests, six of the ten home countries have five firms or fewer in the sample. Countries can be clustered by size (GDP) to provide a higher level of aggregation into three groups, where country = {large, medium, small}. A rough categorization based on GDP as an indicator of market size generates the following clusters. The US is the only large country with a 1990 GDP in $US of 5.5 trillion. France, Germany, Italy and the UK qualify as medium, with 1990 GDPs in $US of 1.2, 1.5, 1.1 and 1.0 trillion, respectively. The Netherlands, Spain, Switzerland, Canada and Sweden

qualify as small with 1990 GDPs in $US of 283, 491, 300, 568 and 229 billion respectively. The dual nationality firms (Sweden/Switzerland, UK/Netherlands) can be clustered as small and medium, respectively, by considering their GDPs collectively ($530 and $1.2 trillion). The average GDP of the country clusters and the average size (total assets) of the firms in each country cluster are given in Table 6.4. The averages suggest a slight relationship between company size and the size of the home country economy, but a non-parametric test based on rank (Kruskal-Wallis) shows that differences in mean size, tested both as absolute and as log values, are far from significant (Chi-square 1.728, significance level 0.421). Although size among this sample of firms does not appear significantly related to home country size, the theoretical arguments in Chapter 4 suggest they will be related to the overall degree of internationalization and internationalization patterns. These relationships will be investigated in subsequent sections.

Table 6.4: Sample size and average firm size, by size of home country (1990)

Country of origin	*# of companies in sample*	*Avg. GDP ($US mil)*	*Avg asset value, 1990 ($US mil)*
LARGE	59	$5.554.100	$27.168
MEDIUM	53	$1.191.255	$26.098
SMALL	10	$374.687	$20.933
Total	**122**	**$1.219.255**	**$26.192**

6.1.3 Sectoral affiliations

The analysis is cross-sectional in that sector was not a selection factor, but there will still be attention for the sectoral affiliations of the companies in the sample. Company activities are usually described by a 2-digit SIC code (UNCTAD) or industry code (Fortune), which provide a quick overall impression of the company's business activities or 'core business'. Table 6.5 shows the sectoral affiliations of the 122 companies in the sample based on their Fortune industry codes (FIC) as they existed in 1990 (which Fortune has modified several times since).

Table 6.5: Sample distribution by Fortune industry code (1990)

FIC	*Description*	*N*	*FIC*	*Description*	*N*	*FIC*	*Description*	*N*
1	Aerospace and Defense	5	17	Food Consumer Products	5	34	Network / Other Comm. Equip.	2
2	Airlines	3	18	Food Production	1	36	Petroleum Refining	12
4	Beverages	2	20	Forest & Paper Products	2	37	Pharmaceuticals	4
5	Building Materials, Glass	1	21	General Merchandisers	8	40	Scientific, Photo, Control Equip.	1
6	Chemicals	7	22	Health Care	1	42	Semicond; other Elec. Comp.	1
9	Computers, Office Equip.	5	23	Household / Personal Prod	1	43	Specialty Retailers	2
10	Diversified Financials	1	24	Industrial & Farm Equip.	5	44	Telecommunications	10
12	Electronics, Elec. Equip.	5	44	Tobacco	2	46	Trading	1
13	Energy	2	30	Metals	2	47	Utilities: Gas & Electric	2
14	Engineering, Construction	1	31	Mining, Crude-Oil Prod.	1	49	Wholesalers: Food & Groc.	2
15	Entertainment	1	32	Miscellaneous	2	50	Wholesalers: Health Care	1
16	Food & Drug Stores	10	33	Motor Vehicles & Parts	11			

There are 35 different industries represented in the sample, averaging an N per industry of less than four. Twelve of the 35 Fortune categories are represented by only a single firm. From an aggregate point of view (e.g. trade flows), defining activities in terms of SIC codes makes sense. From the perspective of individual core companies, however, activities in reality span multiple sectors in the traditional SIC-based segmentation. Based on these considerations, the core companies in the sample were reclassified after a qualitative investigation of additional sources: 1) the 4-digit SIC codes as reported by Dun & Bradstreet's Who Owns Whom (1990/91); 2) the 4-digit SIC codes reported by Worldscope for 1990 (there are slight discrepancies in the level of specificity between the two); and 3) the 'description of business' as reported by Worldscope, which reflects the share of certain activities in revenues as reported in company annual reports.

Companies in Dun & Bradstreet reported anywhere from one to five 4-digit SIC codes. Clustering the firms based on similar patterns in SIC codes showed that certain 'industries' (or product categories) tend to overlap from a company point of view. In many cases, core companies active in e.g. electronics were also active in office equipment, scientific instruments or computers. Companies involved in oil were for example often active in other energy sources such as coal mining and metal ore extraction. The motor vehicle-, aerospace- and industrial equipment industries also exhibit considerable overlap. Volvo, for instance, makes automobiles and industrial equipment; Daimler-Benz makes automobiles as well as airplane engines, and United Technologies supplies parts to both the automotive and aerospace industries. The same can be said of core companies active in food, beverage and tobacco, such as PepsiCo (food and beverage) and RJR Nabisco (food and tobacco).

On the basis of qualitative clustering of the overlap between core company activities, eight 'supersectors' were distinguished based essentially on an aggregation of existing sectors: 1) *motor vehicles, aerospace and industrial equipment (VEHIC)*; 2) *chemicals and pharmaceuticals (CHEM)*; 3) *computers, electronics and scientific equipment (COMP)*; 4) *food, beverages and tobacco (FOOD)*; 5) *retail and wholesale (RETAIL)*; 6) *petroleum, mining and minerals (PETR)*; 7) *utilities, trading and infrastructure (UTIL)* and 8) *construction, engineering, forest products and building materials (CONST)*. This reclustering, based on company activities in 1990, generates sectoral 'superclusters' with an average N of over 15. The smallest sector, construction, engineering, forest and building materials, comprises only six firms and the largest, retail & wholesale, comprises 22 firms. Table 6.6 shows the sectoral clustering of the 122 companies in the sample, where the companies are listed by cluster alphabetically.

Table 6.6: Number of firms by supersector (1990)

VEHIC	*CHEM*	*COMP*	*FOOD*	*RETAIL*	*PETR*	*UTIL*	*CONST*
ABB	BASF	3M	BAT	Ahold	AMOCO	AMR	Bouygues
AlliedSignal	Bayer	Alcatel S.A.	Coca-Cola	American	ARCO	AT&T	BTR
BMW	Dow	Compaq	ConAgra	Stores	BP	BCE Inc.	Georgia-
Boeing	Du Pont	Digital Equip	Ferruzzi	Carrefour	Chevron	BellSouth	Pacific
Caterpillar	Hoechst	Electrolux	Danone	Col. Health /	Elf	BT	Int. Paper
Chrysler	ICI	Ericsson	Nabisco	HCA	ENI S.p.A.	EDF	Pinault-
Daimler-Benz	Johnson &	GE	Nestlé S.A.	Costco	Exxon	Enel SPA	Printemps-
Fiat S.p.A.	Johnson	HP	PepsiCo	Fed. Dept.	IRI	France	Redoute
Ford	Merck	IBM	Philip Morris	Stores	Marathon	Télécom	Saint Gobain
Fried. Krupp	Novartis	Intel	Procter &	Fleming	Mobil	Gen des Eaux	
GM	Preussag	Kodak	Gamble	Franz Haniel	Pechiney	GTE	
Lockheed	Rhône-	Motorola	Sara Lee	Home Depot	RAG	Lufthansa	
Mannesmann	Poulenc	Philips	Unilever	J.C. Penney	Shell	MCI /	
McDonnel-		Siemens AG		J.Sainsbury	Texaco Inc.	Worldcom	
Douglas		Thomson		Karstadt	Thyssen	RWE Group	
Peugeot		Xerox		Kmart	Total	Suez L.	
Renault				Kroger	Usinor	des E. D.	
Robert Bosch				Metro AG	VIAG	Telefónica	
United				Promodès		United	
Technologies				Safeway		Airlines	
Volkswagen				Sears		Veba	
Volvo				Supervalu			
				Target			
				Tesco PLC			
				Wal-Mart			
20	11	16	12	22	18	17	6

An overview of sectoral distribution by country size shows a fairly random pattern, although a few observations stand out. The retail and wholesale sector (RETAIL) is predominant in the large country (the US), suggesting that size in retail is best attained from within a large domestic base (Table 6.7). The second-largest sector in the US is computer, electronics and scientific equipment (COMP), represented by ten firms, followed by vehicles, aerospace and industrial equipment (VEHIC) with nine. Medium-sized economies have a greater representation among petroleum, mining and minerals (PETR), with eleven firms, followed by utilities, trading and infrastructure (UTIL) with nine companies. Half of the ten firms from small economies are active in COMP and VEHIC, followed by UTIL with two and CHEM, FOOD and RETAIL with one each.

Table 6.7: Sectoral representation by size of home country

Size	*VEHIC*	*CHEM*	*COMP*	*FOOD*	*RETAIL*	*PETR*	*UTIL*	*CONST*	*N*
LARGE	9	4	10	7	14	7	6	2	59
MEDIUM	9	6	3	4	7	11	9	4	53
SMALL	2	1	3	1	1		2		10
Total	**20**	**11**	**16**	**12**	**22**	**18**	**17**	**6**	**122**

These observations suggest further that firms in certain sectors are more likely to be international than others. If, for instance, retail is primarily a domestically oriented sector,

it is likely that *ceteris paribus* a retail firm from a small country would not be large enough to meet the primary sample selection criterion of *size* due to the lack of growth potential in a small domestic market. Similarly, the representation of small countries in COMP and VEHIC suggests that these sectors may be relatively more internationalized. The relationship between sector, country and internationalization will be explored in subsequent sections.

6.1.4 Cross-border integration

Although strategic decisions are taken at the firm level, the strategic options available to the firm (as well as previous strategic decisions) are in part driven by sectoral considerations. It is expected that sector will not only be a factor in the 1990 baseline strategy clustering, but also in the post-1990 strategy migrations. The sectoral clustering also forms the basis for the distinction between the cross-border integrated strategies and the multidomestic strategies. In the strategy typology developed in Chapter 4, each geographically oriented strategy type was segmented into those firms whose strategy hinges on vertically integrated production across borders and those with relatively autonomous national units. The former are the *regional division of labor* (RDL), *bi-regional division of labor* (BiRDL) and *globally integrated* strategy (GLOB); the latter are *regional multidomestic* (RMDM), *bi-regional multidomestic* (BiRMDM) and *global multidomesti*c (GLMDM).

Cross-border integrated production as referred to here is the movement of intermediate goods across borders one or more times between stages in the production process. This can involve e.g. shipping parts to destination markets for final assembly, or the import of intermediate goods for final assembly in the home country before final export sales are conducted. Autonomous production in nationally based units means that inputs are sourced, processed and final goods are consumed within the local business and market environment. In practice this may have a micro-regional character (e.g. 'the Benelux') but generally it refers to a fragmented market agglomeration, whereas cross-border integrated production generates relatively more homogeneous goods and where the locus of production and locus of consumption are relatively disjointed.

In the sparse literature on cross-border integration, intra-firm sales are traditionally used as a proxy of measurement (Harzing, 2000; Kobrin, 1991). Although intra-firm sales reporting is an excellent starting point, companies are not uniformly required to disclose the intra-firm share of sales (and even less so its geographic makeup), particularly in European countries (see also Appendix 2). The cross-border integrated character of production is largely a matter of industry. Certain industries, for instance, are known to be highly integrated across borders, such as automobiles and electronics. Others, such as food and other fast-moving consumer goods, tend to be oriented towards national markets. Using available information on intra-firm sales for the firms in the sample, it can be shown that a clear relationship exists between supercluster affiliation and the likelihood to report intra-firm sales (Table 6.8). The supersectors are sorted in terms of the percentage of companies in the cluster reporting intra-firm sales (IFS) and the degree of vertical integration (IFS as percentage of total sales, or TS).

Table 6.8 shows that five superclusters of core companies are, to varying degrees, vertically integrated across borders (shaded rows), namely computers, electronics and scientific equipment (COMP); petroleum, mining and minerals (PETR); chemicals and

pharmaceuticals (CHEM); motor vehicles, aerospace and industrial equipment (VEHIC); and construction, engineering, forest and building materials cluster (CONST). Firms operating in the clusters food, beverages and tobacco (FOOD); retail and wholesale (RETAIL); and utilities, trading and infrastructure (UTIL) are far less likely to report intra-firm sales (seven of 51 combined) and if they do, their intra-firm sales represent a considerably lower share of total sales (on average less than three percent). These considerations will form the basis for allocating firms to the various multidomestic and integrated clusters below.

Table 6.8: Cross-border vertical integration by sector (1990)

	Total N	*Firms w/ IFS*	*Pct of N*	*IFS as % of TS*
COMP	15	12	80%	18.2%
PETR	18	12	67%	9.0%
CHEM	11	6	55%	11.3%
VEHIC	20	7	35%	20.4%
CONST	6	3	50%	6.4%
FOOD	12	3	25%	2.6%
UTIL	17	2	12%	4.2%
RETAIL	22	2	9%	1.3%
	122	**47**	**39%**	**11.8%**

6.2 Dimensions for analysis

In Chapter 4, the theoretical characteristics of two dimensions of core company internationalization strategies were explored: on the one hand, the geographic spread of production activities, and on the other the organizational aspects of strategy. Regional integration is first and foremost a matter of restructuring economic activity through geographic space. The typology of internationalization strategies (Chapter 4) is based solely on the regional characteristics of firms' spatial organization of production. The organizational dimensions will form a basis for analysis, but not the basis for generating regionally-relevant clusters.

6.2.1 Measuring the scale and scope of internationalization

Studying the restructuring of core company activity in an international setting requires a firm-level measure of internationalization. Although FDI has been the primary means by which to (indirectly) analyze firm-level trends, dissatisfaction with FDI has grown in recent years. FDI is not a good indicator of internationalization given its shortcomings for drawing firm-level inferences (Cantwell, 1992; Ramstetter, 1998; Hirst and Thompson, 1999; Vernon, 1998; Hennart, 2000; Stephan and Pfaffmann, 2001; Lipsey, 2001).
An increasing numbers of scholars have considered internationalization at the firm level in recent years (Stopford *et al*., 1992; Dunning and Pearce, 1985; Ramaswamy *et al*., 1996; see also Dunning, 1993). Measuring the significance of location, the value of economic activity, added value or production in a given location underlies the meaning given to internationalization processes and outcomes, and ultimately determines how the

multinational enterprise is conceptualized and defined. Various authors have attempted to develop sound and objective firm-level measures of internationalization (Ramaswamy *et al*., 1996; Sullivan, 1994 and 1996). Three of the more common indicators are sales, assets and employment by geographic area as proxies for the spread of activity.

Firm-level indicators of internationalization are quite diverse and there is little agreement as to their applicability (Ramaswamy *et al*., 1996). Multinationality is a multidimensional concept considered in varying degrees in terms of *operations*, *ownership* or *orientation* (Perlmutter and Heenan, 1979; Anavarjula and Beldona, 2000). Peck *et al*. (1999), for example, address orientation when considering the foreignness or foreign experience of directory boards. Saudagaran and Biddle (1995), on the other hand, deal with ownership issues when looking at company listings on foreign stock exchanges. Yet others measure foreignness in terms of psychic distance to trade and investment destinations, number of subsidiaries abroad as a percentage of the total, or a composite based on multiple variables (Sullivan, 1994).

In terms simply of the significance for a firm of a given location (the *operational* dimension of foreignness), however, three of the more prevalent indicators are foreign sales (FS), foreign assets (FA) and foreign employment (FE) measured as percentages of the total (cf. Oxley and Schnietz, 2001; Kwok and Reeb, 2000), or the Transnationality index (TNI) developed by UNCTAD (a composite indicator based on all three). Often the objective is to link international operations to firm 'performance' (Michel and Shaked, 1986; Daniels and Bracker, 1989; Qian and Li, 1998; Gomes and Ramaswamy, 1999; Lu and Beamish, 2000; Ruigrok and Wagner, 2003; Gestrin, Rugman and Knight, 2001; Goerzen and Beamish, 2002), whereby the nature of that link remains hotly debated.

The three indicators can be criticized because e.g. their firm-specific nature arguably creates difficulties in cross-firm comparison, or that they do not provide accurate representation of true value added. But they do share characteristics of revealing geographic significance for firms, and have been shown to be correlated and effective measures of internationalization (Ietto-Gilles, 1998; Lee and Kwok, 1988; Rugman, 1976). At the same time the three indicators differ in important ways and as such complement each other well in providing a well-rounded overall picture of the spatial organization of a firm's activities. Assets give an indication of a firm's productive capacity or the extent to which it controls economic resources, and the share of a firm's assets in a given location provides an indicator of the importance of that location in the firm's overall strategy. 'The value of capital that TNCs mobilize and control abroad annually in direct investment projects can be approximated by looking at year-to-year changes in total assets of foreign affiliates. The value of these assets reflects funds from sources other than the TNC itself, and as such gives a more accurate picture of the size of annual investments abroad by TNCs' (UNCTAD, 1997: 25).

Sales, on the other hand, are a measure of a firm's output and relative participation in an economy. The foreign sales to total sales (FS/TS) ratio can be viewed as a proxy for a firm's dependence on overseas markets for revenues as well as production. In general it can be viewed as a surrogate for the value of production in the foreign subsidiaries of the MNE and a measure of the geographic scale of international production (Gomes and Ramaswamy, 1999; Ietto-Gillies, 1998; UNCTAD, 1998). The ratio is the most common and widely applied indicator of the multinationality of a MNE (cf. Dunning, 1981), especially in studies analyzing the relationship between multinationality and performance (Sullivan, 1994).

The geographic spread of employment is a similar measure to assets, but it is often a dependent variable to other factors. It provides insight into a MNE's dependence on foreign labor markets and, additionally, captures a firm's socio-economic significance in a way assets do not. Ramstetter (1998) mentions production and employment levels as opposed to FDI, as better indicators or proxy's of the extent of MNE involvement in an economy and level of internationalization. They are not influenced by stock prices, inflation and exchange rates and other fluctuations in the financial sphere. Employment changes in MNEs reflect 'real' output changes not captured by changes in sales (Dunning & Pearce, 1985).

The typology of internationalization strategies set out in Chapter 4 is based in part on the relationship between production and consumption. A domestic firm, for instance, can be measured as one that not only produces domestically but whose products are consumed domestically as well. A company with an export strategy, on the other hand, produces at home but sells its goods abroad, while a multi-domestic firm for example both produces / sources and sells locally. Thus a more relevant approach to firm-level measures of internationalization may be to *highlight* the differences between indicators.

Applying the TNI ratio as a measure of internationalization implies a dangerous step in quantifying a supposed relationship between the three: why should they all weigh equally in a ratio? Perhaps their differences be highlighted to emphasize different aspects of strategy. Certain assumptions already suggest that the three should not simply be thrown together: sales is usually expected to be the most international of the three, because it is easier to export from the home country before producing locally. Assets lag behind because e.g. R&D and higher technology production tends to be kept closer to home. Employment is often even less international because the mobility of labor is less than the mobility of (fixed) capital, and again less than the mobility of goods. Moreover, the distinction between sales by country of origin and sales by destination markets is often overlooked (see also Appendix 3). Whereas the former is likely to be related to assets shares since it reflects the value of production in a given location regardless of its destination, the latter reveals little about the location of production but rather where the goods are consumed.

Since assets can be seen as a proxy for a firm's productive activity (Gomes and Ramaswamy, 1999; UNCTAD, 1998; Sullivan, 1994), a change in the relative importance of a geographic location should be reflected in a change in relative sales shares. In other words, relative divestment (investment) should be evidenced by a decrease (increase) in the relative value of sales (i.e., output) generated from a given location over time. In practice (see Appendices 2 and 3), firms do not provide geographically structured accounts of their assets, sales by origin, sales by destination and employment. Of the 122 firms, only just over half report both sales and assets data.

6.2.2 Measuring organizational aspects

Studies of internal organization date from the 1960s and 70s (Chandler, 1962; Perlmutter, 1969). Such studies dealt with the development of company organograms as a response to strategic shifts. As the emphasis shifted in the late 1980s to the role of knowledge in organizations, studies refocused on the flow of information and the allocation of decisionmaking capabilities within firms (Bartlett and Ghoshal, 1989), generally conducted at the case level. Recent studies consider the role of firms in 'external' networks, i.e. in

their relationships with other firms, be it through joint ventures, technology alliances, or supplier linkages (Andersson and Johansson, 1997).

As a matter of 'internal' networks, organizational complexity can be seen as a function of the characteristics of a firm's subsidiary base. As Ietto Gilles (1998) points out, information concerning the spread of assets, sales etc. across relatively highly aggregated geographic segments says little about the degree to which that activity is concentrated in multiple 'agglomerations' in space. Yet in International Business literature, information on the location of company subsidiaries as measures of internationalization and strategy has thus far only been employed sparingly. The Harvard Multinational Enterprise Program (Curhan and Davidson, 1977) pioneered the field through its documentation of the foreign affiliates of US multinationals since the early 1900s. More recently, Ietto Gilles (1998) developed a 'network spread index' based on the number of countries in which firms had subsidiaries for a large sample of firms. Additionally, she developed a Herfindahl index to measure the *concentration* in various locations. The network spread index (NSi) is also addressed by UNCTAD (1998).

The aforementioned studies employ subsidiaries as a measure of internationalization, but not as a measure of organizational complexity, largely because the *relationships between subsidiaries* are lacking. Subsidiaries do not stand alone in a given host country. Rather, they are woven into a web of ownership patterns that can be both broad and deep. Moreover, these hierarchical relationships exist both within and across borders. So whereas total subsidiary base can be used as a measure of organizational complexity, the breadth and depth of that complexity, in addition to its cross-border character, provide much greater insight into issues of organizational structure (see also Chapter 4).

Breadth refers to the 'horizontal' relationships within a firm's corporate tree, primarily the number of first-level subsidiaries under the parent. These subsidiaries may represent holdings, divisions, or completely distinct businesses, and the more there are the wider the scope of strategic considerations and strategic vision that must be managed within the organization. Depth refers to the level of hierarchy in an organization – a relatively 'shallow' organization, with only first-level subsidiaries that fall directly under the global parent will likely require less coordination effort than an organization whereby those first-level subsidiaries also have several levels, or layers, of subsidiaries below them.

The cross-border character of the network is not simply the number of countries (network spread) in which the company has subsidiaries. It refers rather to the likelihood that any given subsidiary falls under a subsidiary in a *different* country. Conceptually that likelihood can be equally high for a subsidiary base spread across two countries as for a subsidiary base spread across 20 countries; as such it is distinct from strict measurements of subsidiary internationalization. Considered together, however, it remains plausible that more host countries has a 'multiplier' effect on complexity through the introduction of additional cultural, political and social exigencies that condition strategy.

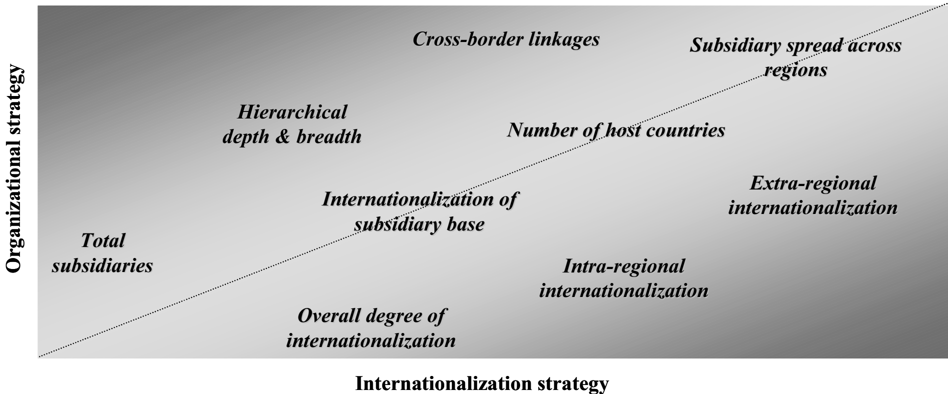
Subsidiary-based data can be complementary to asset- and sales data. Subsidiary data tends to be more detailed than assets and sales, given at the level of individual countries ('Luxembourg') as opposed to geographic regions ('Western Europe') and thus refining the geographic spread based on assets and sales alone. At the same time subsidiary data provides virtually no information as to the size or importance of any given subsidiary, so the value or significance of its location can only be derived from the total number of subsidiaries in that location. For a sufficiently large sample, however, it can be expected

that, *ceteris paribus*, concentrations of subsidiaries will be positively related to concentrations of assets.

6.2.3 Variables for analyzing internationalization and organization

To measure internationalization and organizational structure, a number of indicators will be used. While internationalization in most International Business literature is primarily looked at in terms of 'foreign' vs. 'domestic' activities, a more detailed geographic segmentation will be more revealing, giving insight into not only the *scale* of internationalization, but also its *scope* (Van den Berghe, 2003). The scope of internationalization emphasizes the regional role in strategy, measuring the intra- and extra-regional character of internationalization. The asset- and sales data along with the subsidiary data create three categories of variables that will be used in the analysis: *internationalization*, *network spread* and *organizational structure*. (Figure 6.1). Foreign assets will be used to measure the overall degree of *internationalization* (as a share of total). Foreign activity will then be broken down into its intra- and extra-regional composition. *Organizational structure* will be measured in terms of a firm's total subsidiary base, the depth and breadth of its subsidiary network, as well as the cross-border character of subsidiary relationships (although organization based solely on subsidiary network is relatively one-dimensional, measurement in this way can not only be more easily linked to the production variables, it is also a good measure of complexity in managing and coordinating strategy within a core company). The *network spread* will be measured in terms of the overall degree of internationalization of the subsidiary network, the number of host countries and the degree of concentration / dispersion through geographic space. The network spread variables in essence form a bridge between the other two variable types (symbolized by the dotted diagonal in Figure 6.1).

Figure 6.1: Measuring international strategy



The point of departure for the initial classification is the scale and scope of internationalization, measured initially in terms of geographic distribution of production / productive capacity (assets).

The following definitions apply:

1) XRP
   The extra-regional share of production (XRP) refers to the share of production located outside the home (geographic) region as proxied on the basis of asset shares (in percent). Where asset values are not available, employment figures are used. In cases where neither are available, sales by country of origin (see Appendix) are used. XRP is an indicator of the relative geographic ('global') dispersion of activity.

2) DOIP
   The Degree of Internationalization of Production (DOIP) refers to the internationalization of production as proxied by the international share of assets (in percent). Where asset values are not available, employment figures are used. In cases where neither are available, sales by country of origin (see Appendix 2) are used. DOIP is an indicator of the relative importance of foreign activity.

For additional information on data collection and methodology, see Appendix 2. The aforementioned variables are described here as they apply to all the strategy types and thus provide the foundation for discriminate analysis. Additional variables will be introduced as needed based on their relevance for specific subsets and, indeed, certain strategy types. Descriptive statistics for the internationalization variables are presented in Table 6.9.

Table 6.9: Descriptive statistics, internationalization variables (total sample)

	N	*Minimum*	*Maximum*	*Mean*	*StDev*
XRP	122	0.0%	71.3%	19.0%	18.3%
DOIP	117	0.0%	97.0%	28.0%	23.5%

The maximum values reveal extremely high degrees of internationalization as well as extra-regional production. The average values are considerably lower, at 28 percent international activity (DOIP) and an extra-regional share of just 19 percent (XRP). The standard deviations are on the one tail of the distribution close to the zero value for both variables and on the other tail, just over half the maximum value (51 and 38 percent, respectively). This skewness suggests a bias in the sample towards relatively low levels of internationalization, which will be explored further below.

6.3 Quantifying international strategies

Ordering the companies in the sample according to their respective strategies will take place by non-statistical hierarchical clustering. The primary variables by which to categorize firms by strategy involve various measures of internationalization. The internationalization and organization variables are related in a strategy feedback loop (see Chapter 3), but since in this case the coordination strategy is in essence a response to the degree of internationalization (and other factors), internationalization will be leading and to a certain extent coordination will be deduced indirectly from the internationalization

variables. Moreover, certain variables apply only to certain strategies and therefore function as 'switches' in allocating firm to certain categories.

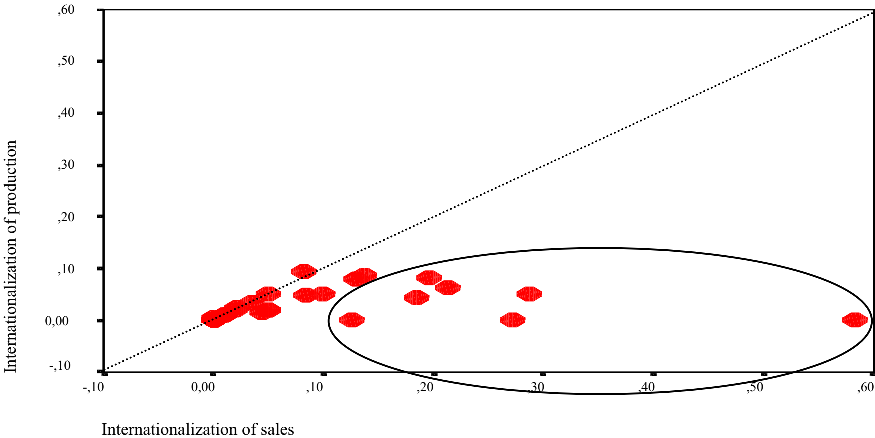
6.3.1 Domestically oriented strategies

Checking the sample for firms with a degree of internationalization equal to zero (DOIP = 0) shows that 17 firms qualify as absolutely domestic. Based on the argument that a firm with no more than 10 percent of its activities abroad effectively qualifies as 'domestically-oriented', an additional 11 firms emerge for a total of 35 firms with an overwhelmingly domestic orientation. In the strategy typology in Chapter 4, such firms can potentially pursue a domestic or export strategy. The latter can be distinguished from the first on the basis of a marked difference between the internationalization of sales and internationalization of production. For the purpose of identifying this distinction, the following variable is introduced:

3) DOIS
   The Degree of Internationalization of Sales (DOIS) refers to the internationalization of sales as proxied by the international share of sales by destination (in percent) i.e., to final markets. Given that the strategies quantified in the current study rest in large part on the difference between production and sales activity, DOIS was measured (where possible) as sales by destination. In cases where sales by destination were unavailable, sales (by origin) to third-party customers were used. The latter case thus includes exports from the home country but excludes intra-firm sales (see Appendix 2).

The first step is therefore to identify those firms with foreign sales share (DOIS) that is markedly different from foreign production (DOIP). A simple scatter plot (Figure 6.2) shows that of the 35 domestically oriented firms, seven show a marked difference (circled), meaning that the DOIS value is at least twice the DOIP value. Among these seven firms, the airline industry formed the core group (AMR, United Airlines, Boeing and McDonnel Douglas) alongside heavy industrial groups IRI, Veba and RAG.

Figure 6.2: International production vs. sales, domestically oriented core companies (1990)



The average values for the primary variables per strategy subset are shown in Table 6.10.

Table 6.10: Scale and scope of internationalization, domestically-oriented core companies (1990)

	N	*XRP*	*DOIP*	*DOIS*
DOM	28	0.6%	2.1%	1.1%
EXP	7	1.5%	3.4%	22.3%

The domestically oriented core companies are listed in Table 6.11. Note that the question of cross-border integration is not relevant given the lack of cross-border production in general.

Table 6.11: Domestically oriented core companies (1990)

	DOMESTIC		***EXPORT***
American Stores	France Télécom SA	Nabisco	AMR
BellSouth	Georgia Pacific	RWE Group	Boeing
BT	Home Depot	Sears & Roebuck	IRI
Columbia Healthcare	J.C. Penney	Supervalu	McDonnel Douglas
ConAgra	Karstadt	Target	RAG
Costco	Kmart	Telefónica	United Airlines
Electricite De France	Kroger	Tesco PLC	Veba
Enel SPA	Lockheed	Wal-Mart	
Federated Dept. Stores	MCI Worldcom		
Fleming	Metro AG		

6.3.2 Regionally oriented strategies

Identifying the regionally oriented strategies is relatively straightforward. The low-end parameter for the degree of internationalization was set at greater than 10 percent (DoI>10%), thereby excluding the 33 domestically-oriented firms, and the high-end parameter was less than ten percent outside the home region (XRP<10%). However, this leaves open the possibility of Company A with a DOIP of 11 percent and an extra-regional share of 9 percent, which technically qualifies but clearly does not reflect an RDL strategy. To control for such a possibility, an additional variable was defined as:

4) RORP
   The Rest-of-Region share of production is the percent of the total (measured as the share of total assets) located in the rest of the home region. For the both regionally-oriented strategies, the relevant parameter was established such that RORP had to account for *at least half* of the DOIP (note that RORP + XRP = DOIP).

The home region for NAFTA core companies was defined as comprising the US, Canada and Mexico, while the home region for European core companies was defined more generally as 'Europe' (cf. Dunning, 1997a), given that different firms use different definitions and in most cases EU (EC) was not reported as a geographic segment. Moreover, an EC figure in 1990 would have omitted 5 of the 'EU15' and generated an organic leap in the longitudinal analysis to follow. Thus it is possible that the RORP variable overstates the fact for European core companies, but it is estimated that a maximum possible distortion on (average) would be less than five percent given that not all firms are active in all (particularly non-Western) European countries and that FDI in Europe outside the EU15 is less than ten percent of total European FDI.
These criteria generate a subset of 16 regionally oriented core companies. Since companies can be multidomestic within a region or integrated across borders (RMDM versus RDL), a further distinction between the RDL and RMDM strategies should ideally be made on the basis of a dummy variable indicating the reporting of cross-border vertical integration. The sectoral affiliations of the 16 firms (see section 6.2) were used to distinguish between RMDM and RDL strategies. Two of the firms were active in retail and wholesale (Safeway and Promodès) and one in food (Groupe Danone), sectors designated in section 6.2 as having little to no cross-border integration. These three were classified as regional multidomestic (RMDM). Of the remainder, seven were active in vehicles, aerospace and industrial equipment (Fiat, Chrysler, Daimler-Benz, Peugeot, Renault, BMW, Mannesmann and Krupp); two were active in petroleum, mining and minerals (Thyssen and Usinor); one was active in chemicals and pharma (Preussag); one in utilities, trading and infrastructure (BCE); one in computers, electronics and scientific equipment (Alcatel) and one in construction, engineering, forest and building materials (Pinault-Printemps-Redoute). These thirteen firms were classified as RDL. Values are shown in Table 6.12.

Table 6.12: Scale and scope of internationalization, regionally-oriented core companies (1990)

	N	*XRP*	*DOIP*	*RORP*
RDL	16	6.5%	21.3%	14.9%
RMDM	3	1.0%	35.8%	34.7%

On average, regionally-oriented firms are anywhere from a quarter to one-third international, with the bulk of that international activity in the home region and on average only five percent located outside the home region. The list of core companies by strategy follows in Table 6.13.

Table 6.13: Regionally-oriented core companies (1990)

	RDL		*RMDM*
Alcatel S.A.	Fried. Krupp	Renault	Groupe Danone
BCE Inc.	Mannesmann	Thyssen	Promodès
BMW	Peugeot	Usinor	Safeway
Chrysler	Pinault-Printemps-Redoute		
Fiat S.p.A.	Preussag AG		

6.3.3 Bi-regionally oriented strategies

In a theoretically modeled ideal world, a bi-regional strategy would be characterized by a 50-percent split in activities across two regions. The strategic reality of the firms in the sample, however, showed a considerable slant towards the home country and region. As a result, the application of a 50-percent extra-regional cut-off led to the exclusion of a large number of firms which otherwise fit the bi-regional description, both quantitatively and qualitatively. This generates the following variables:

5) RG2
   The share of total activity located in the second region. In practice, the 'second region' is always North America or Europe for firms based in Europe or North America, respectively.

Essential to the bi-regional aspect is the ability of a second region to account for the XRP.

6) XR2
   The share of extra-regional activity (XRP) accounted for by the second region (RG2), such that XR2 = RG2/XRP. For example, a firm may have an XRP value of 50 percent. If the second region has a share of 25 percent, the second region accounts for half of all activity outside the home region (XR2=50%). Hence the lower the value of XR2, the less concentrated the firm's extra-regional activity is.

XR2 turned out to be highly discriminating. Whereas the second region (for all firms with at least 30 percent extra-regional activity) accounted for on average 61 percent of extra-regional activity, bi-regional firms exhibited XR2 values of 80 to 90 percent (Table 6.14). As for regionally oriented strategies, the sectoral affiliations also led to clear distinctions between the bi-regional multidomestic (BiRMDM) and bi-regional division of labor (BiRDL) strategies.

Table 6.14: Scale and scope of internationalization, bi-regional strategies (1990)

	N	*XRP*	*DOIP*	*RORP*	*RG2*	*XR2*
BiRDL	8	39.0%	48.5%	8.8%	31.0%	79.8%
BiRMDM	4	47.7%	51.4%	3.7%	44.1%	91.4%

Four of the firms were active in chemicals and pharma (Dow, Du Pont, Rhône-Poulenc and Johnson & Johnson). Another four were active in the computer, electronics and scientific equipment sector (3M, Compaq, Digital Equipment and IBM). One was active in petroleum, mining and minerals (Pechiney), one in food, beverages and tobacco (Sara Lee) and two in retail and wholesale (Franz Haniel and Ahold). Based on their sectoral affiliations, the latter three were classified as BiRMDM firms. Of the remaining nine companies, all but one were classified as pursuing a BiRDL strategy. The exception, Johnson & Johnson, was classified as a BiRMDM because it, of all the chemical and pharma firms in the sample, is the most oriented towards final consumer products and works through franchising, licensing and local production strategies (Table 6.15).

Table 6.15: Bi-regionally-oriented core companies (1990)

BiRDL		*BiRMDM*
3M	Du Pont	Franz Haniel
Compaq	IBM	Johnson & Johnson
Digital Equipment	Pechiney	Ahold
Dow	Rhône-Poulenc	Sara Lee

6.3.4 Globally oriented strategies

For the most highly internationalized strategies, it proved possible to maintain an extra-regional percentage (XRP) of 50 percent as guideline. On that basis nine firms were eligible. All were highly internationalized, on average more than 70 percent. Of the extra-regional component, less than half could be attributed to a single other region (XR2), indicating a solid spread of activities across three regions or more. As in previous cases, sectoral affiliation formed the basis for classification into the subtypes 'globally integrated' (GLOB) and 'globally multidomestic' (GLMDM) (Table 6.16). Four firms operated in the petroleum, mining and minerals sector (Exxon, BP, Mobil and Shell), and one (BTR) in construction, engineering, forest and building materials (in fact BTR is also linked to the petrochemical industry through its plastics and rubber production). These firms were classified as globally integrated (GLOB). The remaining four firms were all active in food, beverage and tobacco (BAT, Coca-Cola, Nestlé and Unilever) and were classified as globally multidomestic (GLMDM).

Table 6.16: Scale and scope of internationalization, globally oriented strategies (1990)

	N	*XRP*	*DOIP*	*RORP*	*RG2*	*XR2*
GLOB	5	56.2%	68.0%	12.9%	23.6%	43.3%
GLMDM	4	60.6%	81.1%	21.1%	30.1%	51.1%

The four GLMDM firms were highly internationalized (over 80 percent) with an extra-regional share of just over 60 percent. The GLOB firms were slightly less extra-regional and also relatively less rooted in the home region and the second region. Their rest-of-region share was markedly lower than that of the GLMDM companies, and the role of the second region was also less pronounced. The companies are listed in Table 6.17.

Table 6.17: Globally oriented core companies (1990)

GLOBAL		*GLMDM*	
BP	Mobil	BAT	Nestlé
BTR	Shell	Coca-Cola	Unilever
Exxon			

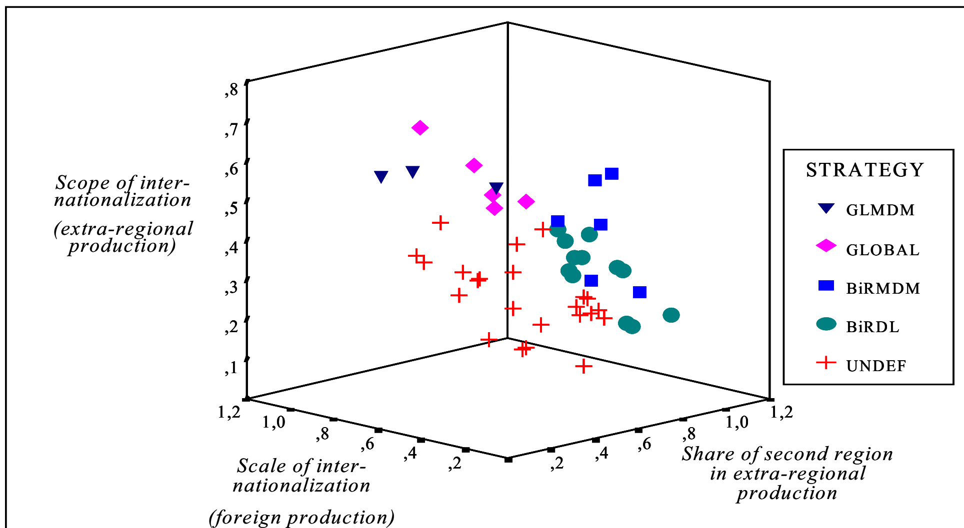
6.3.5 Transitional strategies

In the analysis, 50 companies (nearly 41 percent) did not adequately fit the criteria of any strategy type, due to a number of reasons:

a) some firms were too international to qualify as domestic but that international activity had no discernable geographic focus (no clear regional dimension);
b) some firms were too extra-regional to be purely 'regional', but at the same time not bi-regional;
c) some firms exhibited extra-regional shares comparable to the bi-regional firms but lacked a sufficient second-region focus to be clearly bi-regional;
d) some firms had a (lack of) second-region focus comparable to global firms but were simply not sufficiently extra-(bi)regional to qualify as global

Figure 6.3 shows how the 'unallocated' firms relate to the other strategy types in terms of the three key dimensions analyzed thus far: extra-regional activity (XRP), degree of internationalization (DOIP) and the role of a second region (XR2). In the figure the global strategies are positioned at the top and somewhat to the left (i.e., back along the XR2 axis) and the bi-regional strategies centered and to the right, indicating a lower XRP but a higher XR2 value. The undefined firms occupy the center of the figure, below and to the left of the others.

Figure 6.3: Transitional strategies relative to bi-regional and global strategies (1990)



Although these 50 firms could be described as hybrid on the basis of their dual-strategy characteristics, a better designation would be 'transitional'; i.e., in between strategy ideal-types. Their departure from the well-fitting characteristics of the typology should be seen in the context of the dynamic nature of strategy. A desire to squeeze firms into a

straitjacket of ideal-types runs the risk of imposing a degree of stasis on strategy which is artificial.

To highlight the transitory nature of strategy, the decision was taken to allocate the remaining firms to the subset of the strategy type which provides the best fit. In practice this flows directly from the criteria *a* through *d* described above. The group defined by criterion *a* comprises eight companies with a foreign component (DOIP) ranging from 10.7 percent to 21.3 percent, and an average of less than two percent for the rest of the home region (RORP value). Firms of this type are classified as ‘Domestic plus’ (DOM+), based on the fact that they are highly domestic with a relatively large yet unfocused foreign component (ARCO, AT&T, ENI, GE, GTE, Sainsbury, Lufthansa and Marathon).

The largest cluster (35 firms) of the transitional subset had an average internationalization value (DOIP) of nearly 38 percent, comprising on average 13 percent over the rest of the home region (RORP) and an extra-regional component (XRP) of 24 percent (criterion *b*). For the higher XRP values, the XR2 share was very low across the board, thus excluding a possible bi-regional classification. These 33 firms were classified on those grounds (criteria *b* and *c*) as ‘Regional plus’. Of the 33 firms, 28 were active in vertically integrated sectors and were labeled RDL+. Four operated in chemicals and pharma (Bayer, BASF, Novartis and Hoechst); five in computers, electronics and scientific equipment (Ericsson, Intel, Kodak, Siemens and Xerox); three in construction, engineering, forest and building materials (Bouygues, International Paper and Saint Gobain); six in petroleum, mining and minerals (AMOCO, Chevron, Elf, Texaco, Total and VIAG); and ten in vehicles, aerospace and industrial equipment (ABB, AlliedSignal, Caterpillar, Daimler-Benz, Ford, GM, Robert Bosch, United Technologies, Volkswagen and Volvo). The remaining seven, classified as RMDM+, were active in food, beverage and tobacco (Ferruzzi, Philip Morris, Pepsi and Procter & Gamble); utilities, trading and infrastructure (Gen. des Eaux and Suez Lyonnaise des Eaux) and retail and wholesale (Carrefour).

On the basis of criterion *d*, seven firms exhibiting degrees of internationalization averaging over 55 percent and an average extra-regional share of activity of 40 percent were classified as ‘Bi-regional plus’. In addition to relatively higher extra-regional and internationalization indicators compared to the bi-regional cluster, the ‘plus’ group exhibits an XR2 share of 41 percent (cf. the 80-plus percent average for the ‘true’ Bi-regional cluster). The ‘plus’ therefore refers conceptually to the inclusion of either a third region or some diffuse additional activity, but without attaining sufficient presence outside the first two regions to qualify as ‘global’. All seven qualified as BiRDL+ on the basis of their sectoral affiliations. Two were active in chemicals and pharma (Merck and ICI) and the remaining five in computers, electronics and scientific equipment (Electrolux, Hewlett-Packard, Motorola, Philips and Thomson. The 45 companies are listed by transitional strategy subtype in Table 6.18.

Table 6.18: Transitional strategies, 1990

TRANSITIONAL STRATEGIES				
DOM+	RDL+		RMDM+	BiRDL+
ARCO	ABB	Int. Paper	Carrefour	Electrolux
AT&T	AlliedSignal	Intel	Ferruzzi	Hewlett-Packard
ENI S.p.A.	AMOCO	Kodak	Gen des Eaux	ICI
GE	BASF A.G.	Novartis	PepsiCo	Merck
GTE	Bayer AG	Robert Bosch	Philip Morris	Motorola
J.Sainsbury	Bouygues	Saint Gobain	Procter & Gamble	Philips
Lufthansa	Caterpillar	Siemens AG	Suez L. des E. D.	Thomson
Marathon	Chevron	Texaco		
	Daimler-Benz	Total		
	Elf	United Technologies		
	Ericsson	VIAG		
	Ford	Volkswagen		
	GM	Volvo		
	Hoechst	Xerox		

In order to generate a sense of relativity, table 6.19 compares the key variable values for each 'plus'-cluster with those of its 'true' counterpart. For simplicity's sake the integrated-versus-multidomestic characteristics are not applied and clusters are grouped by geographic orientation (RDL and RMDM, BiRDL and BiRMDM, and GLOB and GLMDM are clustered as 'regional', 'bi-regional' and 'global' respectively).

Table 6.19: Scale and scope of internationalization, 'plus'-clusters versus original clusters

	N	*XRP*	*XR2*	*DOIP*	*RORP*
DOM	35	0.8%		2.3%	1.6%
DOM+	8	12.5%		14.2%	1.7%
REG	16	5.4%		25.0%	19.6%
REG+	35	23.3%	63.6%*	37.7%	14.7%
BiREG	12	41.9%	83.6%	49.5%	6.9%
BiREG+	7	40.1%	40.9%	55.2%	15.2%
GLOBAL	9	58.1%	46.8%	73.6%	16.5%
TOTAL	**122**	**19.1%**	**61.3%**	**28.1%**	**10.0%**

**N=32*

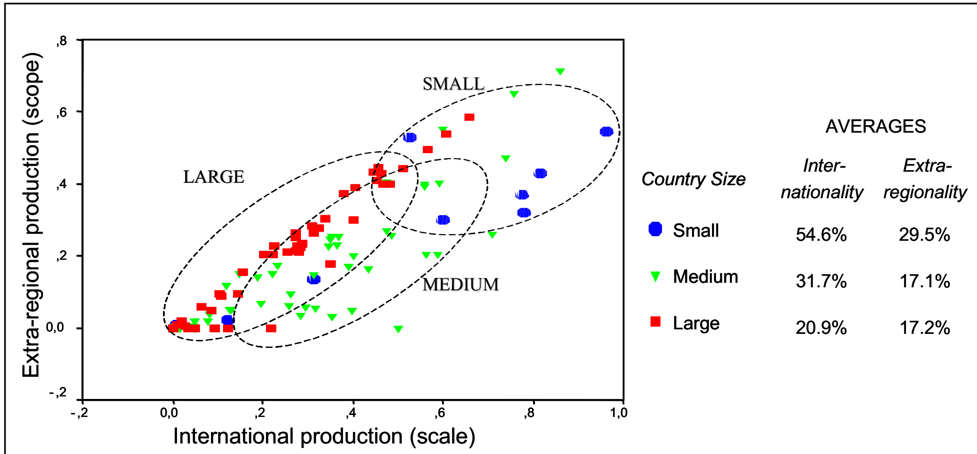
The differences between the original clusters and the 'plus' clusters (gray rows) are readily apparent in Table 6.19. The 'domestic plus' group clearly shows a higher degree of internationalization than the domestic cluster, yet that internationalization is largely extra-regional and rarely specified geographically in the relevant companies' annual reports, indicating that it refers to a relatively diffuse, regionally-unspecific pattern of international

activity. The 'regional plus' cluster is also considerably more international than the regional firms, and again its higher degree of internationalization (DOIP) is largely extra-regional while the XR2 variable (the share of the second region in extra-regional total) shows a low second-region focus. The bi-regional plus category also exhibits international and extra-regional characteristics similar to the bi-regional group yet exhibit a much lower second-region focus.

6.3.6 Home country and sectoral affiliations

It is possible that internationalization, and thus the strategy clustering, is related to the country of origin and / or the sectoral affiliations of companies in the sample. Testing for a relationship between strategy and country of origin is difficult due to the different, and relatively small, sample sizes per cluster and per country of origin. Countries were grouped in section 6.2 by overall size into three clusters (small, medium and large countries). Firms were grouped by the three clusters in a scatter plot to show differences in degrees of overall internationalization (DOIP) and extra-regionality (XRP) for all firms (Figure 6.4). Included are also the average values per cluster and their general position is indicated by the three dotted ovals.

Figure 6.4: Country size and internationalization (1990)

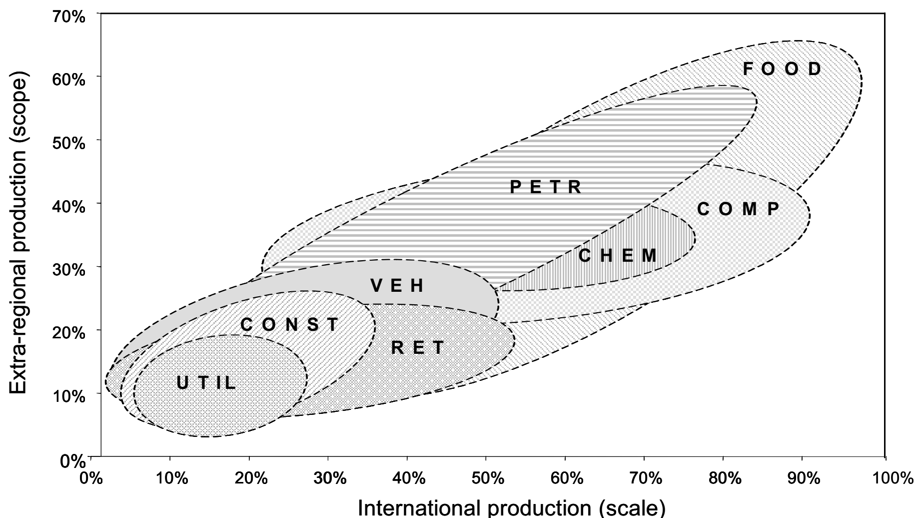


Despite the diversity overall, the figure convincingly shows that firms in the sample from smaller countries (except Spain's Telefonica) are clearly more international than firms from other countries. Core companies from medium sized countries (UK, Germany, France and Italy) are more international than firms from large countries (i.e., the US), but less extra-regional. Firms from these countries are more focused on their home region, while US companies operate relatively more outside the home region. This is clearly related to the larger size of 'host country' Europe compared to 'host country' North America, which represents only two small economies (Mexico and Canada).

A Kruskal-Wallis (non-parametric) test of the three country clusters shows that internationalization is significantly different at the 0.01 level (Chi-square 13.874) and extra-regionality is significantly different at the 0.10 level (Chi-square 4.766). The medium-sized and large-country subsets can be compared in a one-way ANOVA due to their larger and similar sizes (53 and 59 firms, respectively). Internationalization (DOIP) is significantly different at the 0.01 level (F-statistic 7.282), while extra-regionality is not significantly different (F-statistic 0.201). From a home-region perspective, therefore (as opposed to home country), the two subsets are comparable. Since firms from medium-sized countries (measured as the natural log of total assets) are not significantly larger than firms from large countries (F-statistic 1.223), it can be concluded that European firms are able to compete with US firms in terms of size by being more international in their home region. As regional firms, therefore, the two are in balance.

An investigation of internationalization by sector also shows clearly identifiable patterns. The scatter of firms by sector is shown in Figure 6.5 by a series of ovals of diverse sizes which represent the general distribution but do not cover the occasional outlier. Sectors like service, trading and infrastructure are relatively domestic in nature, reflecting the nationally segmented markets of e.g. telecommunications and utilities. Retail is also oriented primarily at the home country, in which (as shown above) the US as a home market figures prominently. Construction, engineering, forest and building materials (CONST) as well as vehicles, aerospace and industrial equipment (VEHIC) have a clear regional orientation while chemicals and pharma (CHEM) and computers, electronics and scientific equipment (COMP) have a stronger extra-regional presence. Firms in food, beverage and tobacco (FOOD) and petroleum, mining and minerals (PETR) show a much wider range of internationalization, with some firms being clearly regionally oriented and others highly globalized.

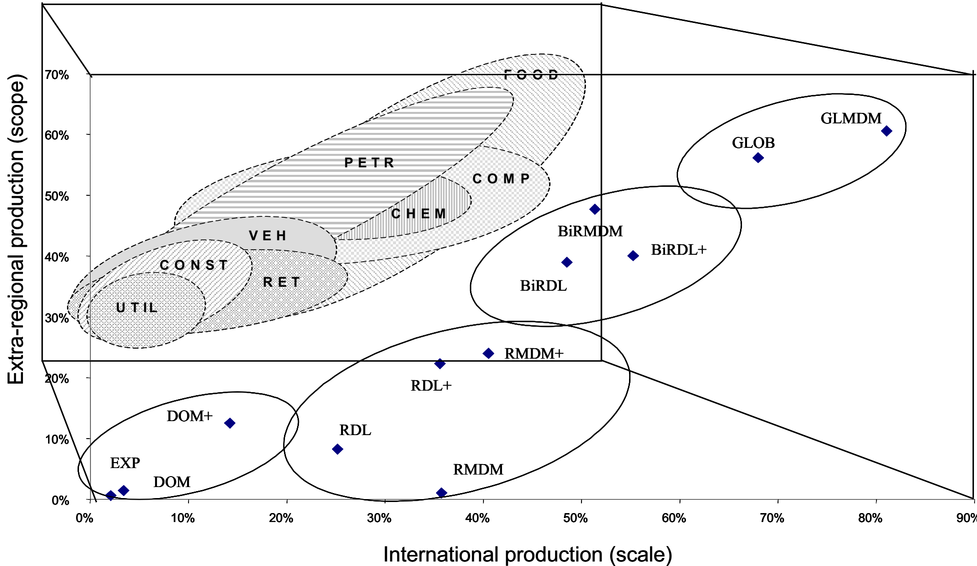
Figure 6.5: Internationality and extra-regionality by sector (1990)



6.3.7 Overview and additional analysis

Figure 6.6 visualizes the relative (average) positioning of the various strategies along the two most important dimensions, scale and scope. The axes in Figure 6.6 are ordered from high to low in terms of the expected relative positioning of each strategy type, with 'global' being the most international and 'domestic' the least. The figure is not intended to suggest a linear *trajectory* as it represents a static situation. The relative internationality and extra-regionality of the strategy clusters is superimposed upon the same dimensions by sector to make explicit the interrelationship between the two.

Figure 6.6: Internationality extra-regionality by strategy type and sector (1990)



In essence the mean values relate to each other as expected. Striking is that the three multidomestic strategy types are relatively both more international and (where applicable) more extra-regional than the global, BiRDL and RDL strategies, respectively. This may point to a relatively larger decentralization of coordination among the former. Moreover, multidomestic firms can be distinguished across the board from their integrated counterparts on the basis of the difference between the internationalization of production (DOIP) and the internationalization of sales (DOIS). Integrated firms have much higher DOIS values relative to their DOIP, indicating that sales is relatively more internationalized than production, while multidomestic firms have production and sales figures that are not only on average closer together, but often exhibit an inverse relationship, i.e. a relative decentralization of production relative to sales (Table 6.20). GLMDM firms form an exception in that their sales are more international than production.

Therefore, although production and sales are highly correlated over the sample as a whole (see 6.2), the data suggests that the degree of correlation depends firstly on whether a firm's production is integrated across borders or not as well as on the degree of internationalization. Finally, in light of the 'global' and 'footloose' hype which emerged in the debate on MNEs in the late 1980s, it deserves mention that only nine (7.3 percent) of the 122 largest US and European manufacturing firms qualified as 'globally oriented' in 1990. By far the overwhelming majority (94) was either oriented towards the home country or at best the home region (DOM through RMDM+).

Table 6.20: Average values for primary variables, all strategy subtypes (1990)

	N	DOIP_90	DOIS_90	RORP_90	XRP_90	RG2P_90	XR2_90
DOM	28	2.1%	3.2%	1.5%	0.6%		
EXP	7	3.4%	25.7%	1.9%	1.5%		
DOM+	8	14.2%	24.9%	1.7%	12.5%		
RDL	13	22.5%	42.5%	16.2%	6.4%		
RMDM	3	35.8%	30.9%	34.7%	1.0%		
RDL+	28	37.6%	48.4%	14.5%	23.6%	14.3%	60.9%
RMDM+	7	37.8%	36.8%	15.5%	22.3%	18.4%	78.3%
BiREG	8	48.5%	57.2%	8.8%	39.0%	31.0%	79.8%
BiRMDM	4	51.4%	44.4%	3.7%	47.7%	44.1%	91.4%
BiREG+	7	55.2%	66.9%	15.2%	40.1%	16.7%	40.9%
GLOB	5	68.0%	70.3%	12.9%	56.2%	23.6%	43.3%
GLMDM	4	81.1%	85.3%	21.1%	60.6%	30.1%	51.1%
Total	122	28.1%	36.0%	10.0%	19.1%	17.8%	61.3%
Chi-square		*80.359***	*63.215***	*47.048***	*91.122***	*47.949***	*25.494**

***Significant at the 0.001 level; *Significant at 0.01 level. (Kruskal-Wallis)*

Kruskal-Wallis Test conducted for N=100; subset 'DOIP=0' excluded

6.4 Network spread and organizational characteristics

The analysis of core company organizational structures (breadth, depth and cross-border linkages) will be combined with the analysis of network spread given that both dimensions build on the same data set. The data for these dimensions are drawn from the Who Owns Whom volumes 1, 3 and 6 (1991) from Dun & Bradstreet (see Appendix 2b for more information on data and data collection). Of the 122 firms, 11 were not available in the Dun & Bradstreet data (all with DOIP = 0) and two were unreliable because of their dual-country character (Shell and Unilever).

6.4.1 Network spread variables

The network spread variables, constructed from the subsidiary data, are drawn largely from Ietto-Gilles (1998). The following three variables are used:

7) DOISUB
   Degree of internationalization as measured by the share (measured as percent of the total) of subsidiaries found outside the home country; an additional qualification of DOIP.

8) HOSTC
   Network Spread (NS) provides a qualification of the DOIP variable by showing the number of countries in which a core company has legally incorporated, majority-controlled subsidiaries.

9) HERF
   A Herfindahl index based on the relative spread or concentration of subsidiaries (a qualification of XRP and XR2) across 6 geographic regions: Northern America, Latin America, Europe, Africa, Asia and Oceania.

   This generates the equation $Hi = \frac{\sum_{1}^{k} X_{ij}}{\left(X_i\right)^2}$

   where X_i equals the total number of affiliates, X_{ij} equals the number of affiliates in region k, with the world consisting of (1…*k)* regions.

Descriptive statistics can be found in Table 6.21. The firms in the sample show on average a high degree of subsidiary internationalization, with approximately half located in a foreign country. Considering that average DOIP values are considerably lower (ca. 30 percent), it can be concluded that on average, foreign subsidiaries are smaller than domestic subsidiaries. The Herfindahl index, given that it reflects concentration over a possible six regions, has by definition a minimum possible value of .167, which indicates completely even dispersion of subsidiaries across regions. The maximum value (1.000) means that all subsidiaries are located in one region. Although the minimum realized value (.252) is low, the average (even discounting domestic firms) is fairly high, meaning that one region (the home region), figured predominantly in core company strategies anno 1990.

Table 6.21: Descriptive statistics, network spread variables (1990), N=109

	Minimum	*Maximum*	*Mean*	*StDev*
DOISUB	0.0%	95.2%	51.3%	26.1%
HOSTC	0.0	77.0	26.0	17.8
HERF	0.252	1.000	0.581	0.219

Based on the assumption that the correlations between the variables would be unduly influenced by the relatively large subset of firms with zero values across all variables (i.e., domestic firms), the set was filtered first for DOIP = 0, and again for DOIP < 10. Normal Q-Q plots for all variables supported the assumption of normal distribution. The results of the latter correlation analysis (N = 81) are presented in Table 6.22.

The correlation matrix clearly shows the interrelated nature of the various internationalization measures. Correlations between variables were moderately strong (and highly significant) across the sample. As would be expected, a higher share of extra-regional activity would imply a higher degree of internationalization, and the international production variables are related to the number of countries in a firm's network and the share of its total subsidiary base abroad. Similarly, the first four variables are negatively correlated to the Herfindahl index, which returns lower values for higher values of the remaining variables.

Table 6.22: Correlation matrix, internationalization and network spread variables (1990), N = 81

	DOIP	*XRP*	*DOISUB*	*HOSTC*	*HERF*
DOIP	1.000				
XRP	0.761**	1.000			
DOISUB	0.459**	0.387**	1.000		
HOSTC	0.460**	0.382**	0.552**	1.000	
HERF	-0.277*	-0.540**	-0.622**	-0.599**	1.000

**Correlation is significant at the 0.001 level (One-way ANOVA, 2-tailed).
*Correlation is significant at the 0.05 level (One-way ANOVA, 2-tailed).

6.4.2 Organizational structure

The subsidiary-based data is thus shown to be sufficiently related to internationalization of production such that organizational variables can be meaningfully defined and analyzed across strategy subtypes. These include the number of subsidiaries, the number of levels in a firm's hierarchy (depth), the share of first-level, or primary, subsidiaries (breadth), the average number of subsidiaries per host country, and the extent of cross-border linkages in the subsidiary network. The variables are defined as follows:

10) TOTSUBS
The total number of majority-owned subsidiaries, considered to be an expression of organizational complexity.

11) MAXLEV
The highest level in a corporate tree; i.e. the 'depth' of the hierarchy. Hierarchical depth is also expected to be an expression of organizational complexity.

12) PRIM
First-level subsidiaries (directly under the parent) as a percentage of TOTSUBS

13) CBL
The chance that any given subsidiary has a parent in a different country. The most important expression of organizational complexity as it focuses specifically on the cross-border linkages between subsidiaries.

The mean values per strategy type are presented in Table 6.23. The organizational variables do not show an immediate pattern, but the range across strategies is quite high. For the sample as a whole, the average firm network consists of 213 subsidiaries, of which just over a third are first-level subsidiaries (PRIM), and core company networks are on average no deeper than five levels. Furthermore, approximately one in three ownership linkages between subsidiaries is across borders while two thirds of all subsidiaries have a parent in the same country.

Table 6.23: Organizational variables, all strategy subtypes (1990)

	N	TOTSUB	PRIM	MXLEV	CBL
DOM	19	56.4	51.1%	3.5	16.0%
EXP	6	266.5	38.5%	4.8	18.2%
DOM+	7	166.3	21.7%	5.0	24.4%
RDL	13	236.9	25.8%	4.6	41.1%
RMDM	3	39.0	65.2%	2.7	31.4%
RDL+	28	270.2	36.1%	4.6	44.5%
RMDM+	7	244.3	22.4%	6.9	27.3%
BiREG	8	135.9	51.7%	3.6	59.9%
BiRMDM	4	241.8	56.6%	4.0	44.3%
BiREG+	7	260.7	24.7%	5.0	43.3%
GLOB	4	574.3	10.4%	9.0	24.5%
GLMDM	3	268.3	28.5%	6.3	46.4%
Total	109	213.7	36.6%	4.7	35.3%

The total number of subsidiaries by strategy type appears fairly random, suggesting that network size is determined by other factors than overall internationalization and extra-regionality. The percentage of first-level subsidiaries in the network does appear inversely related to network size, indicating logically that a larger network is at least in part created through depth as opposed to increased breadth alone. Yet as is the case with depth (MXLEV), there is clearly no obvious one-on-one relationship between hierarchical breadth and network size. There does, however, appear to be a slight relationship between internationalization and cross-border linkages (CBL), as increasingly international strategy clusters generally exhibit a higher degree of the latter. This is not surprising, as a more extensive geographic spread of activities in itself necessitates a more extensive host country base and more borders across which subsidiaries can potentially be linked.

The relationships between dimensions of organizational structure, as well as the link to network spread, can be seen in a standard correlation matrix (Table 6.24). In addition to the established relationship between the network spread variables (DOISUB, HOSTC and HERF), the matrix shows for instance that a larger number of subsidiaries (TOTSUB) does not necessarily mean they are more likely to be international (DOISUB). Although the correlation is significant, the coefficient is quite low. A larger subsidiary base is more strongly correlated with a higher number of host countries, but that inclusion of additional host countries does not mean that expansion in those countries takes place on the same scale as expansion in existing host countries or even the home country.

More relevant for the analysis are the weaker correlations and low coefficients between variables that reflect network spread and those that reflect network organization, such as the lack of correlation between cross-border linkages (CBL) and network size (TOTSUB). This means that organizational complexity in terms of sheer size does not indicate an increased likelihood that organizational links are across borders. As expected, CBL is clearly related to the network spread variables that measure an explicit international dimension, such as DOISUB and HOSTC (the more international the subsidiaries are, the more likely links are going to be across borders) but there is apparently no connection with *size, depth (MXLEV) or breadth (PRIM)*.

Table 6.24: Correlation matrix, network spread and organization variables (1990)

	TOTSUB	DOISUB	HOSTC	HERF	MXLEV	PRIM	CBL
TOTSUB	1.000						
DOISUB	0.275**	1.000					
HOSTC	0.660**	0.712**	1.000				
HERF	-0.250**	-0.786**	-0.721**	1.000			
MXLEV	0.621**	0.232*	0.409**	-0.288**	1.000		
PRIM	-0.415**	-0.110	-0.262**	0.147	-0.736**	1.000	
CBL	0.027	0.800**	0.555**	-0.707**	-0.108	0.151	1.000

**Correlation is significant at the 0.01 level (One way ANOVA, two-tailed)

*Correlation is significant at the 0.05 level (One way ANOVA, two-tailed)

These observations confirm the expectation that organizational complexity is not strictly a matter of internationalization *per se*. It was established in Chapter 4 that in theory, organizational complexity should be related first and foremost to the degree of decentralization of control, i.e. a firm's tendency to pursue a cross-border integrated strategy or a multidomestic strategy.

6.4.3 Cross-border complexity: multidomestic versus integrated firms

In Chapter 4 the theoretical foundations for different organizational structures between firms were found in the different control strategies inherent to the multidomestic approach and the explicit need for cross-border coordination in internationally integrated firms. The organizational variables provide excellent insight into the differences in organization between the two, both in terms of the geographic makeup of their networks and their cross-border character.

It was established above that the internationalization and network spread variables are correlated. The correlations between internationalization and organization are reflected in the network spread variables for individual strategy clusters (Table 6.25). The table shows there is a general rise in the degree of internationalization of the subsidiary base from domestically oriented to globally oriented firms. Similarly, the number of host countries per strategy cluster shows a staggered climb from just 6.8 for the least internationalized firms to over 44 for global multidomestic companies. The Herfindahl index of concentration (HERF) runs from relatively concentrated (0.801) to relatively dispersed (0.317).

Table 6.25: Network spread, all strategy subtypes (1990)

	N	DOISUB	HOSTC	HERF
DOM	19	19.5%	6.8	0.801
EXP	6	22.7%	13.5	0.807
DOM+	7	37.1%	21.3	0.588
RDL	13	52.7%	26.3	0.661
RMDM	3	55.5%	6.0	0.861
RDL+	28	63.0%	35.7	0.466
RMDM+	7	48.2%	23.7	0.601
BiREG	8	79.3%	34.9	0.373
BiRMDM	4	56.3%	29.3	0.545
BiREG+	7	72.7%	36.9	0.427
GLOB	4	69.7%	39.8	0.393
GLMDM	3	76.8%	44.3	0.317
Total	109	51.3%	26.0	0.581

The Herfindahl index also clearly illustrates the difference between the ‘plus’ strategies that emerged from the transitional group and the original clusters. RDL firms, for instance, had a HERF value of 0.661, while RDL+ firms had a HERF value of 0.466. The lower HERF value reflects the extra-regionality inherent in the ‘plus’. Similarly, RMDM firms had a HERF value of 0.861 and RMDM+ firms had a HERF value of 0.601. The BiRDL+ cluster, on the other hand, does not reflect the same trend.
Equally striking is the difference in host countries (HOSTC) between integrated and multidomestic strategies. Multidomestic firms appear active in a considerably smaller number of host countries, and have less diffuse subsidiary networks, than integrated firms. In all likelihood this reflects the higher threshold for multidomestic expansion strategies in which the organization must be replicated more or less integrally in the host country, as opposed to the patchwork nature of strategies built on cross-border integration. By clustering the firms in the sample as ‘integrated’ (INT), comprising RDL, RDL+, BiRDL, BiRDL+ and GLOB firms, and ‘multidomestic’ (MDM), comprising RMDM, RMDM+, BiRMDM and GLMDM, these apparent differences can be explored more systematically (Table 6.26).

Table 6.26: Network and organization variables, integrated vs. multidomestic strategies (1990)

	N	TOTSUB	DOISUB	HOSTC	HERF	PRIM	MXLEV	CBL
INT	60	264.2	64.5%	34.0	0.486	32.9%	4.8	44.4%
MDM	17	211.7	56.4%	25.5	0.584	39.1%	5.4	35.4%

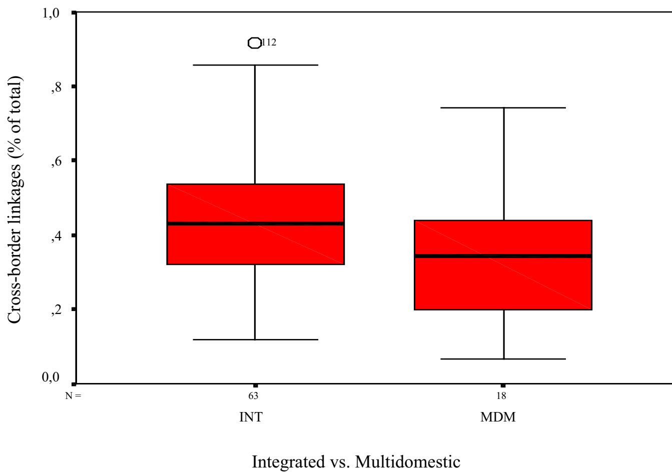
The table shows that multidomestic firms have on average fewer subsidiaries but also a significantly smaller host country base than integrated firms. This means they have relatively deeper hierarchies within their host countries, which reflects the greater embeddedness that is associated with locally responsive multidomestic strategies, where

activities are relatively centralized *within* a given country. Multidomestic firms also have hierarchies with greater depth and breadth than integrated firms, with not only a higher MXLEV value but also a higher PRIM share.

The fact that multidomestic firms have more first-level subsidiaries but fewer foreign subsidiaries in general (DOISUB) suggests that a relatively large share of multidomestic first-level subsidiaries are located in the home country and therefore have a different function than the first-level subsidiaries of integrated firms. Integrated firms have relatively fewer first-level subsidiaries, but more of these are located abroad, which reflects the complexity of organizing production across borders. These first-level subsidiaries function as strategic go-betweens, linking production activities in host countries to the strategic vision of the parent.

The difference in cross-border linkages is the most interesting of all. On average a given subsidiary from an integrated firm has a 44 percent chance of being owned by a parent in another country, whereas for multidomestic firms that likelihood is only 35 percent. This is what one would expect, and also the most important of the variables in that it explicitly considers organizational complexity in terms of cross-border linkages as opposed to e.g. the number of subsidiaries. Since average values can be misleading, the values are shown in a box plot (Figure 6.7).

Figure 6.7: Cross-border linkages, integrated vs. multidomestic strategies (1990)



The plots in Figure 6.7 show that subsidiaries of integrated firms are much more likely than subsidiaries of multidomestic firms to be interlinked across borders. At the same time, multidomestic firms are more likely to have better established hierarchies in a relatively smaller number of host countries. Together these observations provide a clear expression of the different coordination mechanisms pursued under integrated and multidomestic strategies.

6.4.4 Organization by country of origin and sectoral affiliation

The plots in Figure 6.7 show that subsidiaries of integrated firms are much more likely than subsidiaries of multidomestic firms to be interlinked across borders. This difference is a clear expression of the different coordination mechanisms pursued under integrated and multidomestic strategies. In previous sections, it has been established that internationalization and extra-regionality are to varying degrees related to the size of the home country. This will likely also be the case for the network spread variables as well as the organization structure variables.
Table 6.27 shows the network spread and organizational variables by size of the home country economy for the total available N of 109. The three country subsets exhibit both similarities as well as differences. The first observation is that overall subsidiary network size appears to be inversely related to home country size. Firms from the smallest countries have subsidiary bases which are twice the size of the average subsidiary base for firms from the large country, while firms from medium-sized countries fall in between the two. Internationalization in terms of the overall subsidiary base, its geographic spread and the number of host countries is only a distinguishing characteristic in particular for the small-country firms, but it has already been established that this subset of firms is more international than both the subsets from large- and medium-sized countries. In terms of overall organizational structure, the similarities between depth and breadth are found among large- and small-country firms, with medium-sized country firms exhibiting a distinctly narrower and deeper hierarchy. Despite its subtlety, this similarity is an important indication that the small countries in the study (particularly the Netherlands in Europe as well as Canada) have concepts of control more closely related to the US's micro-Fordism than the macro-Fordism of their medium-sized European brethren (cf. Chapters 3 and 4). The likelihood of cross-border linkages between subsidiaries, on the other hand, is virtually identical for all three subsets.

Table 6.27: Network and organizational variables by country size (1990)

	N	TOTSUB	DOISUB	HOSTC	HERF	PRIM	MXLEV	CBL
LARGE	49	151.7	49.9%	23.2	0.526	42.5%	4.5	34.7%
MEDIUM	50	255.5	50.9%	26.8	0.628	29.5%	4.9	35.6%
SMALL	10	308.3	60.9%	35.4	0.608	43.7%	4.4	36.5%

Sectoral affiliations have already been established in the preceding section, since the integrated / multidomestic dichotomy is based on sectoral considerations. But within those overall considerations, differences may be revealing. For the entire available sample (N=109), the average network spread and organizational structure variables were calculated for the seven (super)sectors identified above (Table 6.28). For purposes of comparison, the integrated sectors (CHEM through PETR) are highlighted in gray and the multidomestic sectors are white. Furthermore, the integrated sectors and the multidomestic sectors are sorted in descending order by degree of internationalization of the subsidiary base (DOISUB).

Table 6.28: Network and organizational variables by sector (1990)

	N	TOTSUB	DOISUB	HOSTC	HERF	PRIM	MXLEV	CBL
CHEM	11	258.6	76.7%	48.5	0.365	42.0%	4.82	54.3%
COMP	16	213.8	72.3%	36.6	0.415	42.9%	4.06	53.1%
VEHIC	20	242.3	55.5%	25.0	0.584	45.2%	4.10	39.4%
CONST	6	318.0	50.7%	26.2	0.552	22.0%	5.83	31.9%
PETR	17	268.6	43.7%	26.6	0.605	15.8%	5.59	29.0%
FOOD	11	207.5	63.7%	30.5	0.475	27.5%	6.27	38.1%
RETAIL	13	56.4	27.2%	4.6	0.841	61.0%	2.62	20.9%
UTIL	15	179.0	25.7%	14.0	0.747	29.6%	5.13	15.8%
Total	109	213.7	51.3%	26.0	0.581	36.6%	4.68	35.3%

Many of the possible observations from Table 6.28 have already been made. The integrated sectors, for instance, clearly have larger subsidiary bases than their multidomestic counterparts. In fact, none of the three multidomestic sectors has an average network as large as the smallest average network for integrated sectors. Although multidomestic sectors have on average lower degrees of network internationalization, FOOD-based firm networks are more international, more dispersed, and involved in more host countries on average than three of the five integrated sectors.

For integrated sectors, internationality of the subsidiary base appears to have a positive correlation to network breadth (PRIM) and a negative correlation to network depth (MXLEV). The positive relation is also expressed relative to cross-border linkages (CBL). These interrelationships show that cross-border vertically integrated strategies are similar in design, even across sectors, such that differences in organizational structure are primarily traced to overall internationalization patterns.

Multidomestic sectors, on the other hand, are less homogenous. Between the three sectors, which are most similar differs for each variable. In terms of network spread, RETAIL and UTIL are the most similar, while FOOD and UTIL are most similar in terms of organization structure. This higher level of diversity is perhaps yet again a sign of the increased responsiveness to local pressures under a multidomestic strategy.

6.5 Strategies in the EU and NAFTA

Building on the preceding analysis of core companies in general and their internationalization strategies and organizational characteristics, the sample can now be divided along regional lines. After briefly comparing and contrasting the two, each regional subset will be dealt with individually. The regional analysis will be addressed only briefly here as it forms the basis for the longitudinal analysis and will be explored in more detail in Chapter 7.

6.5.1 Internationalization and organization variables by home region

Dividing the 122 firms in the sample by home region generates balanced subsets of 62 firms from Europe and 60 firms from North America. For these respective subsets, the primary internationalization indicators as explored above are compared in Table 6.29.

Table 6.29: Scale and scope of internationalization by home region (1990)

	N	XRP	XR2	DOIP	RORP
EU	62	21.0%	57.7%[a]	35.6%	16.3%
NAF	60	17.2%	65.8%[b]	20.7%	3.8%

[a]N=40
[b]N=32

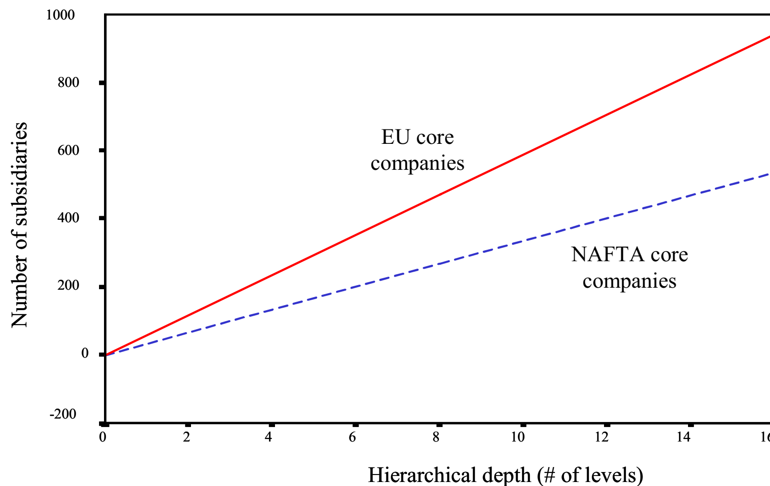
As the table shows, European core companies in 1990 were on the whole more international, and slightly more extra-regional, than their North American counterparts. By conclusion they were considerably more regional in relation to their overall activity. This is not surprising given the fact that the European region is made up of a larger number of relatively smaller countries and the US, home to 59 of the 60 North American companies in the sample, itself accounts for the lion's share of the North American region and thus will account for a proportionally much larger share of regional activity. The RORP data should be qualified, however, in that 'rest of Europe' often includes countries outside the EU15 and the 'rest of North America' on occasion excludes Canada or Mexico (due to data constraints) and is thus a conservative estimate. Strictly speaking, the EU value is probably one to two percent lower and the NAFTA value as much as one percent higher.
For the firms for which it was possible to calculate the share of extra-regional activity accounted for by a second region, the results are also in line with expectations. On average, over 57 percent of European firms' extra-regional activity was located in North America, and nearly 66 percent of North American firms' extra-regional activity was located in Europe. Since both groups were on average close to 80 percent home-region centric in 1990 and over half the remainder was in the other respective region, the conclusion is that on average the two regions accounted for nearly 95 percent of the activities of both European and North American core companies. In other words, the largest Western companies in the world in 1990, taken as a whole, were far from global.
The network spread variables can be considered in conjunction with the organizational structure variables (Table 6.30). As the table shows, the average European core company has a subsidiary base more than 75 percent larger than its North American counterpart (TOTSUB). Since this is not related to a higher degree of subsidiary internationalization (DOISUB), it is likely that the larger network is symptomatic of the macro-Fordist character of production and its higher levels of embeddedness (i.e., more subsidiaries per host country) based on intensive relations with local stakeholders in host (macro-Fordist) countries. Host country embeddedness can also be seen in the greater depth of EU firms (MXLEV). North American firms, on the other hand, not only have shallower hierarchies; they also exhibit a markedly higher share of first-level subsidiaries among their networks, which is characteristic of the micro-Fordist tendency to maintain strategic control close to corporate headquarters.

Table 6.30: All key variables for internationalized companies by home region (1990)

	N	TOTSUB	DOISUB	HOSTC	HERF	PRIM	MXLEV	CBL
EU	59	264.9	52.4%	28.3	0.626	32.3%	4.83	35.8%
NAF	50	153.2	50.1%	23.3	0.527	41.8%	4.50	34.7%

Noteworthy in this vein is that the largest North American firm in terms of subsidiary base in 1990 was Ford, the mother of 'Fordist' production, with 716 subsidiaries. By comparison, the largest European company (BTR) was nearly twice the size of Ford, with 1321 subsidiaries. Even by correcting for outliers through omission of the four European core companies with more subsidiaries than Ford (BP, BTR, ABB and Veba), the EU average is still over 218, i.e. nearly 50 percent larger than the average NAFTA core company. Still, the larger overall network size does not translate into a markedly 'deeper' network structure, given that the average level for EU firms is only a fraction higher than that for NAFTA firms. A scatter plot (Figure 6.8) shows that the slope (see lines on the plot) of the relationship between total subsidiaries and hierarchy depth is considerably steeper for European core companies than for North American core companies, suggesting that larger size in Europe is more related to horizontal expansion of the network than to a deeper, vertical expansion, even *within* countries.

Figure 6.8: Relationship between network size and hierarchical depth, by region of origin



The relative horizontal character of larger size among Europeans is to some extent accounted for by the higher number of countries involved in the network (28 relative to 23). The higher regional concentration (HERF) reconfirms that the higher number of host countries is primarily an intra-regional phenomenon. The cross-border character (CBL) of both subsets was nearly identical at approximately 35 percent, indicating that integration and multidomesticity in strategy are not inherently regional in nature.

6.5.2 Strategy subtypes by region of origin

As suggested above, the differences in average values between the EU and NAFTA samples may have been due to different representation among the strategy types identified in section 6.3. Additionally, firms from the same strategy cluster but different regions may

exhibit different indicator values; e.g., an RDL firm from Europe will likely have a much higher RORP variable than a US-based RDL firm. The makeup of the respective regional samples by strategy type is shown in Table 6.31.

The regional subsets are surprisingly similar in makeup, particularly across the more internationalized segments from RDL+ onwards. The key differences are in the range of domestic through the regional division of labor. North American companies were apparently twice as likely to be absolutely domestic in 1990, as can be argued on the basis of the larger home market. Given a relatively low level of internationalization, NAFTA firms were seven times more likely than EU firms to be 'domestic plus' while EU firms were seven times more likely to pursue a regional division of labor. The data suggest that in the case of a relatively low degree of internationalization, European core companies were most likely to locate in other European countries, whereas North American core companies were most likely to locate outside North America.

Table 6.31: Number of firms per strategy cluster, by region of origin

	DOM	*EXP*	*DOM+*	*RDL*	*RMDM*	*RDL+*	*RMDM+*	*BiRDL*	*BiRMDM*	*BiRDL+*	*GLOB*	*GLMDM*
EU	9	3	3	11	2	16	4	2	2	4	3	3
NAF	19	4	5	2	1	12	3	6	2	3	2	1
TOT	**28**	**7**	**8**	**13**	**3**	**28**	**7**	**8**	**4**	**7**	**5**	**4**

Given the relative similarities between the two regional subsets, the differences in variable values noted above must be due to characteristics of the firms themselves and not differences in strategy makeup of the two subsets. It was established above that, in terms of their *regional* bases, European and North American firms in 1990 were quite comparable.

6.5.3 European core companies' strategic reality in 1990

Although the nine absolutely domestic European core companies show very little country bias (coming from France, Germany, the UK, Spain and Italy), they are relatively sector-specific, based largely in utilities, trade and infrastructure (UTIL), such as Electricité de France, British Telecom, and Telefonica, in addition to the retail and wholesale (RETAIL) companies Metro, Tesco and J. Sainsbury. Exporters (with a strong intra-regional export orientation) were involved in primary industries such as petroleum, mining and minerals (RAG, IRI, Veba).

The intra-regional characteristics of European core company strategies are best exemplified by regionally oriented firms, with an average rest-of-region share of production at just over 20 percent. Some, like Krupp, had only five percent of their total activity located in the rest of Europe, while others, like ABB or Promodès, had rest-of-region shares approaching 50 percent. The 'regional plus' firms had an average RORP value almost identical to that of the RDL firms, but their extra-regional share of activity was over 21 percent on average, compared to less than ten percent for regional firms. At the same time, both the regional and regional-plus groups showed similar patterns of network penetration (majority-controlled subsidiaries) in other EU countries, spanning on average over ten host countries among the EU15+ (including Switzerland) in 1990 (median value also nearly identical at 11). The only difference between the two groups is the extra-regional component, which again demonstrates the accuracy of the 'plus' categorization

since it clearly is additional and does not constitute a substitution effect. It deserves mention, however, that many firms only have one or two subsidiaries in a number of their host countries, and that the penetration rate drops by half (to under six) when per firm only the host countries with at least five subsidiaries are considered.

The inside-out characteristics of geographic dispersion are best expressed in bi-regional strategies as well as globally-oriented strategies. The two European BiRDL firms (Pechiney and Rhône-Poulenc) have comparable levels of RORP as the regional and regional-plus firms, but extra-regional activity in the 40 percent range. That extra-regional activity was located for over 85 percent in North America, where sectoral concerns such as access to mines and minerals were the main factor. The French metals company Pechiney, for instance, had one quarter of its assets in North America in 1990 (primarily Canada and the US) and more than a third of its total sales, while a third of Rhône-Poulenc's production was located in Canada and the United States. The two bi-regional multidomestic firms, Ahold and Franz Haniel, were both retailers with a fairly even split in activities between the home country (the Netherlands and Germany, respectively) and the US.

The four 'bi-regional plus' companies, Electrolux, Thomson, Imperial Chemical and Philips, were all highly internationalized beyond both Europe and North America (as much as 25 percent), whereby Asia played an important role in particular for the latter two. The globally-oriented companies were even more extreme; in the case of Unilever Europe and North America accounted for even less than half of its activities, while Latin America, Asia and Africa all had substantial representation in its network. The most international company in the sample was the global multidomestic Nestlé, over 95 percent internationalized in 1990, with 40 percent of its activity in the rest of Europe and a third outside Europe and North America. The globally integrated companies, Shell, BP and BTR, all (at least in part) British, have a global reach associated with sector-specific needs to source raw materials such as oil and rubber from Oceania, Asia and Africa. BTR, for instance, had 188 majority-owned subsidiaries in the Oceania region in 1990, which constituted 18 percent of all majority owned subsidiaries among the 122 core company subsidiary bases in the region.

Of all European companies, only half had subsidiaries in Mexico. These included particularly chemical companies (BASF, Bayer, ICI, Hoechst), auto manufacturers (VW, Daimler-Benz and Renault) and electronics firms (Philips, Ericcson, Alcatel and Electrolux). The carmakers are all RDL firms and therefore had relatively small operations in Mexico, but chemical and electronics companies are bi-regionally oriented and as such included Mexico in a larger, integrated network. Hoechst, for instance, through its subsidiary Celanese (51 percent ownership), was the largest European-controlled subsidiary in Mexico in 1990 with assets worth nearly two billion US dollars.

6.5.4 North American core companies' strategic reality in 1990

In the US, domestic core companies are overwhelmingly in retail, such as Wal-Mart, Sears, J.C. Penney, and Supervalu. In some cases these firms did, however, have a modest regional presence (on average less than two percent), with more than half of their internationalization having been into Canada or Mexico. Sears and Costco, for example, had internationalized nearly five and ten percent, respectively, within North America by 1990. The two exporters are United Airlines and Boeing. Although the former is in

actuality primarily an exporter of services, Boeing is a clear example of a core company producing nearly all of its product at home but with destination markets around the world.

As noted above, 'domestic plus' is a larger cluster than among European companies. Companies in this category had a low to moderate level of internationalization but without a clear geographic focus, such as General Electric, Atlantic Richfield and USX Marathon. Although General Electric had one of the larger subsidiary bases in Canada and Mexico in 1990 (18 subsidiaries, or six percent of all NAFTA-firm subsidiaries in those countries), but their activities are estimated to have accounted for less than one percent of GE's total production. The remainder of GE's international activity (circa ten percent) was spread across Europe and Asia. ARCO and USX, both in petroleum, mining and minerals (PETR), had somewhat higher levels of internationalization but little to none in Canada and Mexico.

Few NAFTA core companies were purely regionally oriented in 1990. Chrysler is the primary example, having built its network more or less exclusively on a division of labor between the three NAFTA countries. The other RDL is Canada's BCE, with a predominant home presence but more than ten percent of its activity in the US, which accounted for nearly all its international activity. Safeway, with a modest Mexican presence in 1990, qualified as the only RMDM in the sample.

The 'regional-plus' clusters come second only to the domestically-oriented group in terms of cluster size. As in the European case, the 'plus' clearly signifies additional internationalization, because all plus strategies were built on a solid regional platform. In fact, they include not only the largest US core companies outright (GM and Ford) but also the core companies with the largest stake in Mexico, and often Canada as well. Table 6.28 explores the Mexican activities of the ten largest US firms active in Mexico (ranked by Mexican assets). Note that the number four firm, Kimberly-Clark, is not in the current sample and has been included only for the sake of completeness.

Half the companies in the Mexican Top Ten are regional or regional-plus. Table 6.28 shows again the gaping size difference between the US and Mexico, since even these companies, parent to the largest host companies in Mexico, had RORP values of around five percent and in some cases less than one. The list further demonstrates the importance of General Motors, Ford and Chrysler to the region, all three of which pursued strategies centered on the region. Together the ten firms account for over seven billion dollars in assets, eleven billion in sales and more than 100,000 in direct employment. GM alone had just under two billion dollars in assets located in Mexico and over 65,000 employees. Over half their combined output was exported, the vast majority of which went to the United States. These ten firms accounted for nearly half of all Mexican subsidiaries of the 60 US companies (total 125), with the Big Three carmakers accounting for 31 subsidiaries, or one third of the total. Other regional companies absent from the Mexican top ten were more focused on Canada, often as part of a strategy to source raw materials (e.g. Texaco, AMOCO and International Paper). The regional-plus multidomestics (Procter & Gamble, Pepsi and Philip Morris) all had established bases in Mexico in 1990, but considerably smaller than the companies in the top ten list, which all exhibited cross-border integration

Table 6.32: Top 10 US firms in Mexico, 1991 (currency values $US million)

Company	Strategy	Mex. assets	Mex. sales	Mex. empl.	Mex. subs[a]	Export
General Motors	RDL+	1,869	3,382	65,605	22	69.0%
Chrysler	RDL	1,286	2,657	11,383	6	57.1%
Ford	RDL+	1,183	2,996	8,840	13	45.8%
Kimberly-Clark	n.a.	896	923	4,437	n.a.	2.2%
Du Pont	BiRDL	716	272	1,328	1	12.5%
Kodak	RDL+	478	318	3,036	5	30.8%
IBM	BiRDL	418	115	2,145	1	38.1%
Xerox	RDL+	222	317	3,912	3	30.1%
Hewlett-Packard	BiRDL+	144	269	1,024	3	24.2%
Motorola	BiRDL+	50*	153	2,702	3	96.0%
Total		**7,262**	**11,401**	**104,412**	**57**	**49.2%**

Source: Author's calculations based on America Economia and Dun & Bradstreet data

**Estimate*

[a]1990

Smaller-scale Mexican activities were generally part of a strategy with a wider geographic scope (bi-regional to global). The clusters in this range had RORP values as low as one percent and as high as over 18 percent, but were anywhere from 32 to over 50 percent extra-regional. For the bi-regional firms about 80 percent of this extra-regional activity was situated in Europe, while the bi-regional plus and globally oriented firms had similar shares of total activity (i.e., circa 30 percent) in Europe. The 13 companies in the range from bi-regional to global were active in on average 12.4 of the EU15, although if only countries host to at least five subsidiaries are considered, the average drops to less than four, with many companies having only a 'substantial' presence in one or two European countries.

The regional-plus and globally-oriented companies, similar to their European counterparts, had a more sizeable portion (20 to 25 percent) of total activity outside both North America and Europe. Companies in these segments include Hewlett-Packard, Motorola and IBM, as well as two global oil companies (Exxon and Mobil). The most internationalized North American company in 1990 (perhaps intuitively given its brand presence in every corner of the world) was Coca-Cola, with an extra-regional component of nearly 55 percent, just under half of which was located in Asia, Latin America and Africa. By and large, however, it must be reemphasized that even more than for European companies, the geographic scope of North American core company activity in 1990 was centered on the home country or region, and additionally on Europe as a host region. Asia, Latin America, Africa and Oceania on the aggregate represent an almost insignificant share of core company activity, and only a limited case-by-case basis were firms identified for which these regions performed important, let alone central, roles in their internationalization strategies.

6.6 Conclusions

The current chapter quantifies and qualifies the extent and pattern of internationalization, network spread and organizational structure for North American and European core companies in 1990, with the purpose of setting the stage for integration in both regions.

The evidence shows that firms pursued diverse strategies in the run up to integration in the 1990s and that they cannot be discussed in terms of 'the quintessential firm' as is often the case in policy approaches. Strategies of varying geographic scale and scope form a range of strategic realities and in all likelihood a variety of strategic intent with respect to the integration process and outcomes.

The typology as it was developed contains both 'clean' as well as 'plus' categories, which reflects the fact that strategy is fluid and firms are continually in transition. The result is a typology which progresses from absolutely domestic strategies to absolutely global ones. This is not to suggest a strict linear path as the typology does not follow any one firm through time; rather it positions them relative to one another at a given moment (1990). In fact it will be posited in the following chapter that multiple paths or migrations are possible from one position or another.

The typology stresses the importance of a regionally based classification for the analysis at hand. In the literature, the criteria for good strategy typologies are that they should be 1) based on all key strategic characteristics of the entities being classified; 2) hierarchical, consisting of at least two levels; 3) timeless; and 4) parsimonious (Chrisman, Hofer and Boulton, 1988). Such a typology must have a spatial dimension, must describe both intra- as well as extra-regional dimensions. Additionally, the typology must be generalizable to different RIAs, including existing typologies, and be relevant for the structure and analysis of both strategic intent with regard to regionalism as well as realized outcomes. The typology meets these criteria.

The subsets and characteristics of European companies versus North American companies were surprisingly similar. Differences between the sample makeup and the values for the individual clusters are not significant, which makes them comparable subsets and precludes the likelihood that differences in subset composition would distort the analysis. In all objectivity, for both subsets the extent of internationalization in 1990 was fairly limited. The world beyond North America and Europe was only marginally integrated in all but the most internationalized firms' spatial organization of activity. Despite the fad of global and footloose firms that raged in management literature in the late 1980s and early 1990s, only very few if any deserved such a predicate.

Lastly, the typology emphasizes and reveals a number of differences between multidomestic and integrated firms, harking back to debates initiated by Porter (1986) and Prahalad and Hamel. The distinction is clear, not only on the basis of intra-firm sales reporting, but also in terms of the likelihood of cross-border relationships between subsidiaries. Also, multidomestic firms tend to be more international overall, and more deeply embedded in a relatively smaller number of countries than integrated firms. This is logical if, as the concept 'multidomestic' suggests, firms have to replicate their entire structure and decentralize a broader range of functions in their host countries than do integrated companies. The only exception seem to form the global multidomestics, which appear to have enough experience, resources and momentum to build vast multidomestic networks spanning dozens of countries.

7. REALIZED REGIONALISM STRATEGIES OVER THE 1990s

As the second wave of regionalism took shape in the course of the 1990s, core companies had to address and asses their new institutional environment. The management of some core companies had taken an active stance, lobbying directly for (further) broadening and deepening of regional integration, while others adopted a 'wait and see' attitude and some may even have been surprised by the scale of regional dynamism in the 1990s. The political intentions behind (and expectations of) integration in Europe and North America were dealt with in Chapter 5. This chapter analyzes core company strategies longitudinally over the period 1990 through 2001.

First, more 'subjective' dimensions will be examined of the way core companies perceived regionalism to be a strategic issue (section 7.1). The analysis will then move on to more objective measures, also taking into account the way changes to the sample through merger and acquisition (M&A) activity might affect the strategic profiles (section 7.2). The discussion of strategic migrations will be structured by region of origin (section 7.3 on Europe and section 7.4 on North America) and within four larger strategic clusters: domestically oriented, regionally oriented, bi-regionally oriented and globally oriented companies.

7.1 Reflections of regionalism as a strategic issue

The 'game' of strategic intent and strategic reality is played out in part at a rhetorical level. Actors, be they governments or core companies, are keen to present themselves to the outside world in a positive light. While the analysis in this study hinges on a quantitative assessment of realized core company restructuring, it is also important to consider the ways in which companies portray their own restructuring and to what extent they appear to consider regionalism a strategic issue.

7.1.1 Anecdotal testimony of regionalism as a strategic issue

At the anecdotal level, the media and annual reports provide considerable insight into the attitudes of core company management towards integration. Managerial arguments for integration, generally echoed by regionalism's political rationalizations, tend to focus on issues like increased scale and efficiency, increased competition or the benefits of developing regional brands. 'Outsider' firms have traditionally agitated against the dangers of creating regional 'Fortresses'.

US firms, for instance, have traditionally been eager to present themselves as having developed 'a North American focus in … strategy and structure', in most cases involving 'an integration of North American operations' (Blank and Haar, 1998). In some cases this occurred as a 'wave of joint ventures' with Mexican firms, involving e.g. GTE (*Wall Street Journal*: December 21, 1993). Digital Equipment and Daimler-Benz were also acquiring interests to establish pan-European positions (*Computerworld*: July 29, 1991) and US and European chemical companies were 'swapping' assets in Europe to gain scale (*The Economist*: October 3, 1992).

DuPont suggested that the NAFTA led to increased competition, and that as a result 'all of our manufacturing operations must be internationally competitive' (*Business Mexico*: Vol 7/8, issue 12/1, 1998). Shell, meanwhile, centralized decisionmaking in its petrochemical

division to 'better meet customer demand in the [European] single market' (*Chemcal Week*: November 18, 1992) and Renault has been active in closing down less efficient factories in Europe (*The Economist*: March 15, 1997).

Firms from different countries were described as having different approaches to integration. According to a survey by *Business Quarterly* (1995, vol. 59/4), Canadian firms are aiming their restructuring at delivering higher quality and service, while Mexican firms are targeting cost reduction. US companies, on the other hand, are working on lowering costs but also on 'improved supply chain management'. This was described by other sources as the increased integration ('capture') of suppliers in Mexico, for example by Chrysler (*Country Monitor*, April 20, 1994) and BASF (*Purchasing*, February 6, 2003).

European food companies such as Nestlé and Unilever, both ardent supporters of the SEM within the European Round Table of Industrialists, saw potential for the development of European brands (*Marketing*: April 26, 1990). Companies in businesses where consumer tastes differ widely, such as Philips' domestic appliance division, expected gains to come not from product harmonization but from a consolidation of physical distribution. DuPont, Bosch-Siemens and Exxon were also described as having rationalized their logistics and distribution in Europe (*Management Today*: April, 1994). Others, however, used the example of Unilever's increased control of distribution channels to warn against decreased competition under the Single Market (Reynolds, 1995).

Core companies also tended to position regionalization as an alternative to globalization. In the words of Campbell Soup CEO Johnson, 'the strategy for North America is very simple You market locally, manufacture regionally, and source globally – with common technology, knowledge and supplies' (Blank and Haar 1998). Others considered regionalism a stepping stone towards greater regional integration, such as Shell's explicit view that countries like Switzerland and Norway were *de facto* part of Europe from a business point of view (Herkströter, 1996).

Outsiders also had strategic perspectives on integration. In the wake of European integration, 3M announced a drastic restructuring of its European structure (*Business Europe*: November 1, 1993). Swiss companies, with Nestlé and Ciba-Geigy in the lead, were positioned as expanding proactively in EC countries to prevent being locked out in the wake of integration (*Wall Street Journal*: August 31, 1988).

Not all firms were openly positive and some worried that integration would fail to live up to 'the hype' (*Marketing*: April 26, 1991). Many firms argued openly that integration could only be successful behind tariff walls, such as French electronics giant Thomson (*Fortune*: April 20, 1992) and Fiat, Peugeot and Renault (*Wall Street Journal*: November 29, 1990). By 1998, companies like ICI were complaining that the single market was not yet working smoothly (Merriden, 1998). Meanwhile retailers were described as 'taking a wait and see attitude' amid concerns that NAFTA alone is not a recipe for success in entering Mexico and Canada (*Chain Store Executive*, January, 1995). They thereby further nurtured the fear of the real outsiders of European and North American integration of being faced with two increasingly impenetrable 'fortresses'.

More critically, it is not always evident that core company promises of e.g. job creation through integration, on the basis of which the RIA was 'sold' to governments and to the public, ever actually materialized. Public Citizen, for example, published a study in 1997 in which the promise of new jobs through the NAFTA, made in media appearances by dozens of core companies in the run-up to integration, were evaluated ex post. The report concludes that three years into the NAFTA, 60 of the 67 concrete promises they

investigated had been broken. General Electric, for example had testified before the US House Foreign Affairs Committee in October 1993 that sales to Mexico 'could support 10,000 jobs for General Electric and its suppliers'. In 1997, GE was unable to cite any job gains due to trade with Mexico, while the Department of Labor's NAFTA Trade Adjustment Assistance program (NAFTA TAA) certified that GE had laid off 2,304 workers due to NAFTA, nearly all due to a 'shift in production to Mexico'. The strategic rhetoric, therefore, has to be critically evaluated in light of strategic reality.

7.1.2 RIAs in core company geographic segment reporting

Core companies' strategic realities (geographically) are revealed to some extent by the way in which they report their geographic reality. As described in the appendix, publicly traded companies are required by accounting regulations to provide a geographic segmentation of their activities. 'Foreign' versus 'domestic' activities is usually the minimum, while other companies go so far as to list individual countries. Within that range, companies have considerable discretion to segment as they see fit, based ostensibly on differences in market characteristics or perceived risk levels. In general, therefore, individual segments distinguish themselves from others in the segment reporting in that they are considered relatively homogenous in these terms. If it is assumed that RIAs reduce the perceived risk levels between member countries and should lead to more integrated economic structures, it is possible that RIAs lead to increased perceptions of homogeneity by firms and thus that the underlying regions themselves become geographic segments.
A relatively simple analysis of geographic segment reporting in core company annual reports can show whether e.g. 'NAFTA' or 'EU' are included as geographic segments, and whether that tendency increased over the course of the 1990s. Table 7.1 shows the number of firms from both regions which included some form of NAFTA (e.g. 'NAFTA', 'other NAFTA') or the European common market (e.g. 'EEC', 'EC', 'EU', 'SEM', 'other European Community') as a geographic region in the period 1990 to 2001. References to 'North America' and 'Europe', although it is possible they are intended to refer only to the respective RIA member countries, were not included as it was not possible to establish a distinction between those referring to an ambiguous geographic region and those referring to the political region associated with the RIA.

Table 7.1: RIA-specific segments in core company annual reports, 1990-2001

	1990	*1991*	*1992*	*1993*	*1994*	*1995*	*1996*	*1997*	*1998*	*1999*	*2000*	*2001*
EU	17	19	17	14	14	14	14	14	21	22	17	13
NAF									1		1	1

Even keeping in mind that a considerable number of firms in the sample were domestic and thus did not report any segmentation at all, the table still reveals only modest levels of RIA-relevant segment reporting for Europe and virtually no references to the NAFTA. More importantly, there is an absence of a clear positive overall trend, let alone an obvious upswing after 1992. After declining for the mid-1990s, the number of firms referring to Europe as a political entity rose to 22 in 1999 before subsequently declining to 13 in 2001. Although numbers fluctuate because firms change their segmentation over time (becoming in some cases more specific and in others more aggregated; see Appendix II), this is in part also a reflection of a change in sample size due to mergers and acquisitions (see section

7.2). Since 50 of the European core companies were international in 1990, and all but one of the companies reporting ‘EU’ or some version thereof were European (Coca-Cola was the only North American exception), on average is about one third of internationally active European core companies apply an RIA-relevant geographic segmentation.
Despite the ‘regional focus’ proclaimed by many NAFTA companies, that focus has not found its way into their segment reporting. In fact, the one company to report ‘NAFTA’ as a region in 1998 was Fiat, and the 2000 and 2001 references were made by BASF, both European core companies. Analysis did reveal, however, a small number of companies that used the home (geographic) region (‘North America’ or ‘Europe’) as a substitute for the domestic segment. Even given the possibility that this reference includes additional countries (e.g. Norway in the case of ‘Europe’), it clearly suggests a perception of common characteristics among the home country and those in its immediate geographic vicinity (Table 7.2). As such it may reflect a more modest form of incorporating regionalism into the core company’s strategic reality, but one that does not explicate its political dimension.

Table 7.2: Geographic (home) region-specific segments in core company annual reports, 1990-2001

	1990	*1991*	*1992*	*1993*	*1994*	*1995*	*1996*	*1997*	*1998*	*1999*	*2000*	*2001*
Europe	3	4	5	4	6	5	4	3	4	5	6	7
North Am.					1	2	3	3	2	2	2	2

The fact that the tendency to report ‘North America’ as a region arose from 1994 on does suggest that, however small the number of firms, for these firms North American integration was a factor in the formation of a regionally-ordered strategic reality. This small group of firms are incidentally all highly internationalized, such as Unilever, Bayer and Shell, as well as a number of firms that joined the trend at the end of the 1990s like Ahold, Nestlé and Rhône-Poulenc. A more subtle, yet suggestive hint is also given by firms that do not explicitly segment by RIA or substitute the region for ‘home’, but that do alter their reporting in a way suggestive of this recognition. General Motors, for example, reported ‘Canada’ and ‘Latin America’ up through 1991 but in 1992 (i.e., following the signing of the NAFTA) changed its segments to ‘other North America’ and ‘Latin America’, and changed the former yet again in 1996 to ‘Canada and Mexico’. Ford, in contrast, followed the opposite course, by no longer specifying ‘Canada’ as a geographic segment in 1992 and by from 1993 reducing its segmentation to ‘US’, ‘Europe’ and ‘all other’.
Anecdotal evidence of the importance of regionalism as a strategic issue abounds. At the level of geographic segment reporting, however, the regional aspect remains relatively understated. What can be said about actual restructuring, as compared to the rhetoric?

7.2 Restructuring across the sample as a whole

In the current section a number of methodological issues and decisions will be addressed regarding the approach to the longitudinal analysis. The key issues deal with identifying a time frame within which restructuring might be realized and observable, as well as the changes undergone by the sample over time in the form of mergers and acquisitions.

7.2.1 Methodological considerations

In Chapter 6, 1990 was taken as the 'pre-RIA baseline' in order to establish clear periods for a before-and-after comparison. Strictly speaking, for a given RIA, t=0 is the year in which the RIA took effect. For the EU this would be 1993 and for the NAFTA region 1994. According to Jovanovic (2001: 75), however, it should take 'several years' before the dynamic effects of integration in Europe 'such as the restructuring of production' kick in. For the NAFTA countries, on the other hand, an existing *de facto* level of integration since 1987 plus 'shallower' integration make it likely that changes will occur more quickly. On these grounds, the longitudinal analysis was divided into a first period (1991-1995) and a second period (1996-2001), to be analyzed relative to the baseline 1990. Since the variables underlying the data are relatively volatile (currency-based and thus subject to relatively substantial year-on-year exchange rate and valuation fluctuations), the values are averaged out over each period.

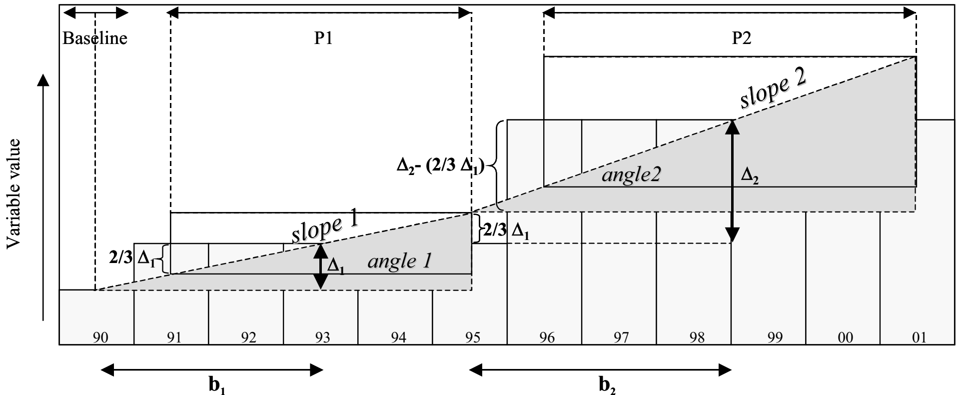
The decision to average is also based on two related considerations that revolve around the problem of missing values. Percentages of e.g. degree of internationalization, or extra-regional activity could not be calculated for all 122 firms for each year. Sometimes this was related to changes in reporting styles, sometimes due to the simple unavailability of reliable data (see Appendix II). In at least 17 cases, missing values after 1997 were related to a merger or acquisition by which the firm simply ceased to exist as a distinct, measurable entity. Therefore for any given year, and increasingly so through time, anywhere from ten to twenty values for a given variable may be missing. The common option in that case is to calculate the averages for the available N each year, assuming the missing values each year are random, from a representative subset of firms and normally distributed. This option was rejected for two reasons.

Firstly, there exists considerable variability across the sample in internationalization variables. The overall degree of internationalization, for instance, ranges from a minimum of 0 percent to a maximum of 97 percent. For the sample of 122 firms as a whole, an average of an available 110 firms per year may be adequate. But since the analysis is based on splitting the sample into region- and strategy-based clusters, using the average values for the sample as a whole will distort the analysis of individual clusters. The average values of other strategy cluster members may be close to hypothetical missing values, but the clusters are too small to generate reliable estimates. An excellent predictor of any of the internationalization variables for any given missing value at time t is the value of the same variable for that firm at t-1. This can be illustrated by using all available foreign asset percentages (the degree of internationalization) for all years from 1990 through 2001.With 1146 of 1342 total possible observations (122 firms times 11 years), the value at t varied on average less than two percent from the value at t-1, with a standard deviation of nine percent. Thus the firm with the missing value at t actually provides a reasonable estimate of its own missing value.

The second consideration involves the issue of mergers and acquisitions (see also below). Since the sample size actually decreases over time due to the acquisition of some companies in the sample by other companies in the sample, averaging values over the sample as a whole for each individual year will place too much emphasis on the overall effects of those acquisitions. The objective of this study is to consider the spatial organization of firms in the period prior to 1995 and the period after 1995, regardless of whether the period after 1995 ended in 1998, 1999 or 2001 for any individual firm. Taking

the average per firm of the second period, no matter how long, diverts undue attention away from the fact that the firm was acquired later in the 1990s. In this way each individual firm is considered equally, and the impact of being *acquired* is downplayed in the analysis while the impact of *acquiring* is highlighted (the acquisition will still be reflected in changes to the values of the acquiring firm). It is explicitly assumed that a firm's strategy under regionalism consists of something more than being acquired.
The internationalization variables have been calculated for three values: **1990 (baseline)**, **avg 1991-1995 (P1)** and **avg 1996-2001 (P2)**. Comparing growth (the 'deltas') between three points in time which are not equidistant is potentially misleading. This is demonstrated in Figure 7.1. The years 1990-2001 are represented by columns of equal width, where the height of 1990 represents the 1990 value, the height of all five columns from 1991-95 represents the average value for that period and the height of the six columns from 1996-2001 represents the average value for that period. The 'delta' between 1990 and the average for 1991-95 is represented by Δ_1, and the difference between the average value for 1991-95 and the average value for 1996-01 by Δ_2. While a direct comparison of the 'deltas' between each of these values provides a general indication of the development in the variable over time, it does not supply possibilities for meaningful interpretation beyond 'increasing' or 'decreasing'.

Figure 7.1: Calculating relative growth over 1990-2001



Ultimately, comparing and contrasting developments across P1 and P2 requires a comparison of the relationship between *growth* from 1990 to P1 and growth from P1 to P2. *Growth* is represented in Figure 7.1 by *slope 1* and *slope 2,* and a comparison of P2 to P1 by the ratio of slope 2 to slope 1. Slopes 1 and 2 are theoretical growth trendlines that pass the averages for both periods at their midpoints. The slope from 1990 (slope 1) crosses 1991-1995 at the period's midpoint (1993) and then continues on through 1995, which also forms the 'baseline' for the period 1996-2001. Slope 2 rises from 1995 to cross the plane of P2 at the midpoint of P2, which is halfway between 1998 and 1999. The ratio of slope 2 to slope 1 can be calculated using laws of right triangles, where *the ratio of slope 2 to slope 1 is equal to the ratio of angle 2 to angle 1*. The angle ratio can be calculated using the tangents of both angles. The tangent of an angle is calculated by dividing the angle's

opposite leg by the angle's adjacent leg. The opposite leg of angle 1 is equal to Δ_1 and its adjacent leg $\mathbf{b_1}$. Since 1993 equals 1990 plus three, $\mathbf{b_1}$ *always equals three*.
The opposite leg of angle 2 is equal to the difference between the value for 1995 (its 'baseline') and the midpoint of P2, halfway between 1998 and 1999 (i.e. 1998.5). This is *not* equal to Δ_2 because Δ_2 is calculated from the average value of P1. The vertical difference between the value at the midpoint 1998.5 and the baseline, 1995, is Δ_2 minus two-thirds of Δ_1. The midpoint of P2, 1998.5, is 3.5 points away from 1995, such that the adjacent leg of angle 2 ($\mathbf{b_2}$) equals **3.5**.
Thus the slope of angle 1 is equal to Δ_2**/3** and the slope of angle 2 is equal to $[\Delta_2-(2\Delta_1/3)]/\mathbf{3.5}$, such that the relationship between slope 2 and slope 1 is:

$$\frac{\textit{slope 2}}{\textit{slope 1}} = \frac{\textit{(tan) angle 2}}{\textit{(tan) angle 1}} = \frac{\mathbf{3}}{\mathbf{3.5}} * \frac{[\Delta_2 - (2\Delta_1/3)]}{\Delta_1}$$

The relationship between slopes over 1990-1995 and 1996-2001 will be used to show acceleration / deceleration trends in the rate of internationalization, termed *relative growth* (RELGR), to compare and contrast trends in the two respective periods under study.
The subsidiary data, on the other hand, have been collected for three distinct time frames: 1990, 1995 and 2001. The data reflect the status of core company subsidiary bases at the end of the year. Although the strategy variables are based on running averages over 1991-95 and 1996-01 respectively and the organization variables on single years (1995 and 2001, respectively), correlations can be expected on the grounds that assets and sales shares, as continuous variables subject to fluctuations and based on figures rounded to the nearest million (in currencies), will generate more reliable and stable figures if averaged over a number of years. It is assumed that individual subsidiaries do not fluctuate as much in absolute numbers nearly as much as they do in terms of their 'dollar' value.
It is also relevant to note that the strategy typology identified in the previous chapter is based on the 1990 values for the variables in question. Analysis over time allows for the possibility that the underlying values change such that a given case remains classified as a given strategy type even though this is no longer the case. For the sake of continuity the clusters will be followed over time, but at the end 'reclassified' according to their most recent data. In this way overall strategy migrations remain the focus. This approach not only preserves the continuity but also allows for a clear comparison between 'before' and 'after', considering not only growth rates but also the baseline position. In this way firms with similar growth rates but different starting points will not necessarily be on the same strategic path.
Given the small sample size relative to the number of clusters (across two home regions), no large-scale abstract modeling is attempted here. The strategy migrations will be dealt with descriptively, delving into the changes and allowing for departures from the 'norm' where necessary. Generalizability is not a problem since the study largely deals with the population of European and North American core companies and is not intended to represent the behavior of firms in general.
The longitudinal analysis will be opened with a discussion of overall trends among the sample. The second step is to discuss the sample in terms of the two central differentiating aspects: region of origin and strategy clusters. In keeping with the exploratory nature of the

study, the discussion over the three dimensions of analysis (scale and scope of internationalization, network spread and organizational structure) will focus on the *salient* aspects as relevant for the various strategies. An analysis of extra-regionality, for instance, is considerably less relevant for domestically- or regionally oriented firm strategies than for bi-regional and global strategies. For the former therefore the emphasis will be more on overall internationalization and *intra*-regionality as opposed to extra-regionality. Additionally, some strategy clusters represent small numbers of firms with potentially divergent strategies. Thus although the analysis will be principally concerned with overall patterns and average values per cluster, where relevant individual cases will be discussed in order to create nuances and make the link to 'real practice'. Before moving to the analysis, the issue of changes to the sample over time will be addressed.

7.2.2 The inclusion of acquired firms in the longitudinal analysis

Since the mid-1990s cross-border M&As have become the primary mode through which internationally operating companies (especially European and US companies) expand abroad. M&As, as opposed to greenfield investments, are considered a fast way for companies to build up a locational portfolio and gain access to foreign markets – not only for inputs and sales growth, but also for tapping into human capital and other forms of 'created assets'. Cross-border (majority held) mergers and acquisitions in the second half of the 1990s increased in number by almost 74 per cent between 1997 and 1998. In 1997 a rise of more than 45 per cent was noted (UNCTAD, 1999) and in 1999 the increase was 35 per cent, reaching – according to UNCTAD estimates - $720 billion in over 6,000 deals (UNCTAD, 2000: 10). Companies in the Core200 were major players in the flurry of M&A activity in the late 1990s. In a small number of cases, M&A activity took place among the Core200. By 1998, 195 of the original Core200 selected in 1995 were left as independent entities. The M&A trend accelerated between 1998 and 2000. Including the M&As up through 2001, the number of core companies eventually left is reduced to 185 (excluding the merger between Chevron and Texaco, which took place nearly at the end of the period under study).

While mergers and acquisitions are grouped together conceptually, only less than 3 per cent are pure mergers (UNCTAD, 2000). Although the distinction is often difficult to identify, acquisitions predominate. In fact many announced mergers are *de facto* acquisitions by stronger partners (e.g. the DaimlerBenz takeover of Chrysler was portrayed as a merger between two equal partners, but in practice quickly turned out to be an acquisition after most of the US top managers left the Board). While the Core200 are major actors in the current M&A wave, they are also subject to takeovers by other corporations – in all but three cases (Vodafone, Albertson's, Bell Atlantic) at the hand of a fellow Core200 company (Table 7.3).

Table 7.3: The impact of the M&A wave on the sample, 1990-2002

Company name	*Country*	*Deal*	*Company name*	*Country*	*Date*	*New name*
Ciba-Geigy	Switzerland	Merged	Sandoz	Switzerland	Dec. 1996	Novartis
Lyonnaise des Eaux	France	Acquired	Cie. de Suez	France	June 1997	Suez Lyonnaise des Eaux
Boeing	US	Acquired	McDonnel Douglas	US	Aug. 1997	Boeing
Compaq	US	Acquired	Digital Equipment	US	June 1998	Compaq
WorldCom	US	Acquired	MCI Com	US	Sept. 1998	Worldcom
Thyssen	Germany	Acquired	Krupp / Hoesch-Krupp	Germany	Oct. 1998	Thyssen Krupp
Daimler-Benz	Germany	Acquired	Chrysler	US	Nov. 1998	DaimlerChrysler
BP	UK	Acquired	Amoco; ARCO	US	Dec. 1998; April 2000	BP
BTR	UK	Merged with	Siebe	UK	Feb. 1999	Invensys
Total	France	Acquired	Petrofina; Elf	Belgium; France	June 1999, Feb. 2000	Total Fina Elf
Albertson's	US	Acquired	American Stores	US	June 1999	American Stores
Carrefour	France	Acquired	Promodes	France	Oct. 1999	Carrefour
Exxon	US	Acquired	Mobil	US	Nov. 1999	Exxon Mobil
Allied Signal	US	Merged with	Honeywell	US	Dec. 1999	Honeywell
Rhône-Poulenc	France	Acquired	Hoechst	Germany	Dec. 1999	Aventis
Vodafone AirTouch	UK	Acquired	Mannesman AG	Germany	April 2000	Vodafone AirTouch
Veba AG	Germany	Acquired	Viag	Germany	June 2000	E.ON
Bell Atlantic	US	Acquired	GTE Corp	US	June 2000	Verizon
Chevron	US	Acquired	Texaco	US	Oct. 2000	ChevronTexaco
Philip Morris	US	Acquired	RJR Nabisco	US	Dec. 2000	Philip Morris

Source: based on Van Tulder *et al*., 2001

Table 7.3 shows that most of the major deals among the Core200 were acquisitions as opposed to mergers. Further, the data show that the majority of all deals are made between core companies from the same country, and only three took place between firms from different regions (BP's purchase of Amoco and ARCO, and the DaimlerChrysler deal). An overview of M&As by size of home country and sector (of the acquired firm) shows that core companies were largely acquired in large and medium countries (eight and seven cases, respectively) and in vehicles, aerospace and industrial equipment (VEHIC) and petroleum, mining and metals (PETR), in which four and seven core companies were acquired, respectively (Table 7.4).

Table 7.4: M&As by sector and size of home country, 1990-2002

Country size	*VEHIC*	*CHEM*	*COMP*	*FOOD*	*RETAIL*	*PETR*	*SERV*	*CONST*	*N*
LARGE	1		2	1		5			8
MEDIUM	3	1			1	2			7
SMALL									
Total	**4**	**1**	**2**	**1**	**1**	**7**			**16**

Table 7.3 reveals only a fraction of the number of acquisitions conducted by companies in the sample over the 1990s. Since companies are constantly buying and selling other companies, being party to a merger or acquisition is not in its own right a basis for excluding any of the companies in question from the analysis. Firstly, nearly all of the companies classified as 'acquired' existed well into the second half of the 1990s, with most being acquired as late as 1999 and 2000. Secondly, patterns in internationalization variables among the 'acquired' subset (ACQ) and the 'survivor' subset (SURV) do not appear materially different, even over time. All four variables (extra-regional production, overall degree of internationalization, rest-of-region production and production in the second region) show generally similar increases from 1990 to 1991-95 and again to 1996-2001 (Table 7.5).

Table 7.5: Internationalization, ACQ vs. SURV (all firms)

	XRP			*DOIP*			*RORP*		
	1990	1991-95	1996-01	1990	1991-95	1996-01	1990	1991-95	1996-01
ACQ	18.6%	22.9%	27.0%	31.7%	37.3%	43.3%	13.1%	14.5%	16.4%
SURV	19.2%	20.7%	23.8%	27.6%	29.9%	35.5%	9.5%	10.8%	13.4%

Although the patterns are similar, the underlying values differ because the acquired companies, in terms of their strategy types, are not representative of the sample as a whole. Of the 15 companies classified as acquired, ten (66.7%) had a regionally-oriented strategy (RDL = 2; RMDM = 1; and RDL+ = 7; RMDM+ = 0), whereas for the sample as a whole less than 42 percent (51 of 122) had a regionally-oriented strategy. This also shows that one in five (20 percent) of all regionally-oriented companies was acquired in the period after 1995 as compared to a ratio of 5 to 78 (6 percent) for the remainder of the sample. In other words, companies with a regionally-oriented strategy were more than three times as likely to be acquired by other core companies as companies pursuing alternative strategies (based on the 1990 classification).

A comparison of the regionally-oriented subsets of acquired and surviving firms may yet show variation, in particularly over time, since the classification that binds the two is based on 1990 internationalization patterns. Table 7.6 shows that the two subsets are very similar in their overall levels of internationalization (DOIP) for all three periods. The only discernable difference is the slightly lower level of extra-regionality of acquired regionally oriented firms compared to their surviving counterparts. If regional orientation itself was indeed a factor in the likelihood of acquisition, it may well be that the likelihood of acquisition was related to the *degree* of regional orientation, even within the bandwidth of the regionally-oriented supercluster.

Table 7.6: Internationalization, ACQ vs. SURV (regionally-oriented)

	XRP			*DOIP*			*RORP*		
	1990	1991-95	1996-01	1990	1991-95	1996-01	1990	1991-95	1996-01
ACQ	15.9%	19.5%	23.5%	33.7%	39.3%	45.8%	17.8%	19.8%	22.3%
SURV	18.1%	20.6%	26.8%	33.5%	37.5%	46.0%	15.9%	17.6%	19.9%

Given that a solid correlation has been established between the organizational variables and the strategy variables (Chapter 6), it is unlikely that organizational and network spread variable values would reveal a different picture. Since the organizational variables are based on one-off values (1990, 1995 and 2001) as opposed to the running period averages of the strategy variables, only the 1990 and 1995 values are available for the firms acquired in the period 1995 to 2001. Table 7.7 shows the network spread variables for the two regionally-oriented subsets. The data, which shows that surviving regionally oriented firms have a greater network spread than acquired regionally oriented firms, support the data in Table 7.6.

Table 7.7: Network spread, ACQ vs. SURV (regionally-oriented)

	DOISUB		*HOSTC*		*HERF*	
	1990	1995	1990	1995	1990	1995
ACQ	46.7%	50.5%	27.7	32.8	0.611	0.608
SURV	60.6%	59.5%	30.5	34.4	0.545	0.541

The third and final argument for including acquired firms in the longitudinal analysis is that ownership change does not directly signal an abrupt departure from a firm's spatial strategy. Chrysler's activities in Mexico, for instance, remain to a large extent what they were prior to the merger with Daimler-Benz. In fact, acquisition may have been Chrysler's best option for the pursuit of an extra-regional strategy given that it was the only of the Big Three without significant extra-regional activity in the early 1990s (after having retreated at the brink of bankruptcy in the 1980s). Whatever the motivation behind an acquisition, acquired firms are not always seamlessly 'absorbed' (cf. De Wit and Meyer, 2003) and the acquired subsidiaries often persist within the new core company network, simply being 'passed on' to new owners. Moreover, these changes and subsequent alterations in strategy and structure under that new ownership, will be reflected in the internationalization and organization of the acquiring firm. Since the same argument applies to all the other acquisitions undertaken over the 1990s that did *not* involve other Core200 companies and are therefore not listed in Table 7.3, there is no reason to omit those acquisitions that did involve other Core200 companies. This is demonstrated by exploring changes between those firms that acquired other core companies (BUYER) and those survivors that did not (OTHER). Variables which may conceptually be expected to show differences such as the total number of subsidiaries, number of host countries, or organizational depth do in fact show no material differences in growth rates between 1995 (pre-acquisition) and 2001 (post-acquisition) (Table 7.8). On the basis of these and the preceding arguments the subset of acquired (and acquiring) firms is included.

Table 7.8: A comparison of growth rates, BUYERS vs. OTHER (1995-2001)

	N	TOTSUB	HOSTC	MXLEV
BUYER	15	21.9%	2.5%	19.8%
OTHER	74	24.2%	2.1%	24.4%

The decision to include the acquired firms in the overall analysis has consequences for the indicator values across the entire sample given the nature of the variables. Since the variables are based on average values over 1991-1995 and 1996-2001, a firm acquired in 1999 will have average values for 1996-01 based on the values for 1996-1998. The acquiring firm's values will be based on the average over the entire period (1996-2001) and thus to some extent the acquisition will be counted 'double' in the overall values for the sample. However, this only creates potential for serious distortion in cases where the acquired firm's strategy (and geographic spread) differs considerably from that of the acquiring firm. In other words, if a firm with 45 percent extra-regional activity acquires another firm with 45 percent extra-regional activity, the average for the new merged firm will still be 45 percent over the period, assuming they are based in the same region. This will for instance be the case for Exxon and Mobil, both global companies in 1990 with similar profiles, or Chevron and Texaco, both with RDL+ strategies. Cross-regional M&As, such as DaimlerChrysler and BP's acquisition of Amoco and ARCO will clearly lead to significant increases in the extra-regional character of Daimler's and BP's internationalization strategy. The effects of ownership change on the composition of the strategy subsets and on individual firms will be discussed in subsequent sections.

7.2.3 Internationalization across the sample

An overview of average changes in internationalization, network spread and organizational structure for the sample as a whole provides a backdrop for the discussion of sectors, countries and strategy clusters. Table 7.9 compares intra-regional and extra-regional internationalization in 1990, 1991-95 and 1996-01. The last two columns represent the difference (deltas) between 1990 and 1991-95, and 1991-95 and 1996-01, respectively.

Table 7.9: Intra- vs. extra-regional internationalization, all companies (1990-2001)

Variables	*1990*	*1991-95*	*1996-01*	*Slope P1*	*Slope P2*	*RELGR*
DOIP[a]	28.1%	30.8%	36.5%	0.92%	1.10%	1.20
RoRP[b]	10.0%	11.3%	13.8%	0.44%	0.45%	1.03
XRP	19.1%	21.0%	24.2%	0.61%	0.58%	0.95

a: N=117 Excludes Shell, Unilever, Novartis, Bayer and Compaq (home region instead of home country)
b: N=116 Excludes Lockheed, for which no regional data were available

On the whole, the sample has become more international, with internationalization contributing both to intra-regional and extra-regional growth. The overall degree of internationalization increased from 28 percent in 1990 to an average of over 30 percent in 1991-95 and over 36 percent in 1996-01. This represents an average rise in the DOIP percentage of about one percent point per year over the decade. The extra-regional share of internationalization increased by just over half a percentage point per year and the intra-regional share by just under half a percentage point, meaning that overall, *extra-regional expansion accounted for a larger share of internationalization than intra-regional expansion*.

The slopes show that the rate of internationalization from 1990-1995 was just *under* one percent per year and just *over* one percent per year from 1996-2001. The ratio of these two slopes is 1.20:1, which shows that the rate of internationalization in the second period was 20 percent higher than the rate in the first period. Despite the larger overall extra-regional push over the decade, the ratios of slope 2 to slope 1 for extra-regional internationalization is below one, which indicates that the rate of internationalization actually *decreased* over the second period. Meanwhile the ratio of slope 2 to slope 1 for *intra*-regional internationalization is higher than one, showing that the rate of internationalization within the home region *increased* after 1995. While overall extra-regional expansion was greater than overall intra-regional expansion in both periods, *the acceleration in the rate of internationalization after 1995 was an intra-regional phenomenon*.

The fact that extra-regional expansion was larger does not necessarily make it more important 'pound for pound'. This is evidenced by the fact that the ratio of rest-of-region activity to extra-regional activity increased from just over 0.52 (10% / 19.1%) in 1990 to 0.57 (13.8% / 24.2%) over 1996-2001 (see Table 7.9). Also, the extra-regional share of the world economy (as a potential target for firms' economic activity) is larger than the intra-regional share of the world economy for firms from both Europe and North America. Focusing on just the second region (North America or Europe as 'host' regions) may help put the extra-regional and intra-regional components of internationalization in better perspective. Table 7.10 shows that activity in the second region (RG2P) as a share of the whole increased only very slightly over the decade (from under 18 percent in 1990 to nearly 20 percent in 1996-01), but that the rate of expansion in the second region *after 1995* was close to zero (0.09 percent). Compared to the rate of internationalization within the home region, expansion aimed at the second region was much more modest.

Table 7.10: The role of the second region in extra-regionality, RDL+ through GLMDM (1990-2001)

Variables	*1990*	*1991-95*	*1996-01*	*Slope P1*	*Slope P2*	*RELGR*
RG2P[c]	17.8%	18.8%	19.7%	0.32%	0.09%	0.27
XR2P[c]	61.3%	60.2%	58.0%	-0.37%	-0.41%	1.10

c: N=72 Excludes companies with less than ten percent production in second region

Expansion in the second region was also much more modest than overall extra-regional internationalization. This is evidenced by the declining role of the second region as a share of extra-regional activity (XR2P) over time. While the second region accounted for over 61 percent of all extra-regional activity in 1990, over 1996-01 that share had been reduced to 58 percent. Thus whereas the second region grew as a share of *total activity*, it accounted for a *smaller share* of overall extra-regionality and was therefore not the *focus* of the extra-regional internationalization thrust. Also, the *deceleration* in growth for second-region activity (RG2P) in 1996-01 relative to 1990-95 means that the *rate of decline* in the importance of the second region (RELGR of XR2P) *increased* from 1996-01 relative to 1990-95. When comparing the home region with the second region, therefore, the acceleration in the rate of internationalization after 1995 benefited primarily intra-regional expansion and came in large part at the *expense* of the second region.

Although the focus in the current study is on the internationalization of production, the analysis can be extended to include changes to the geographic composition of sales activity

for the purpose of comparison. It is possible that changes in the spread of production are accompanied by similar, or contradictory, changes to the spread of sales. With identical constructs as those used to operationalize production, Table 7.11 is the sales equivalent of Tables 7.9 and 7.10 above, with the four bottom rows added to show the difference between the sales and production values. On average, the table shows that sales are more internationalized than production. All variables for 1990, 1991-95 and 1996-01 exhibit values a few percentage points higher than their production counterparts. The gap between production and sales in foreign locations, measured by the –S values minus the –P values in Table 7.11, is shrinking in general terms, indicating that production is internationalizing at a slightly faster rate. This appears to support the incremental theory of internationalization, by which firms serve foreign markets first through sales and gradually increase the scale of local productive activities, observable through a narrowing of the gap between the geographic dispersion of assets and sales.

Table 7.11: Sales versus production, all companies (1990-2001)

Variables	*1990*	*1991-95*	*1996-01*	*Slope P1*	*Slope P2*	*RELGR*
DOIS[a]	36.0%	38.0%	42.6%	0.65%	0.96%	1.48
RoRS[b]	13.4%	14.8%	16.5%	0.46%	0.22%	0.49
XRS	23.9%	24.5%	27.6%	0.21%	0.76%	3.62
RG2S[c]	18.9%	20.2%	22.0%	0.42%	0.27%	0.66
DOIS – DOIP	7.9%	7.1%	6.1%			
RoRS – RoRP	3.4%	3.5%	2.7%			
XRS – XRP	4.7%	3.5%	3.4%			
RG2S – RG2P	1.1%	1.4%	2.3%			

a: N=117 Excludes Shell, Unilever, Novartis, Bayer and Compaq (home region instead of home country)
b: N=116 Excludes Lockheed, for which no regional data were available
c: N=72 Excludes companies with less than ten percent production in second region

The incremental aspect of internationalization by which sales precede production is also shown by the geographic pattern of changes to sales over time. The table shows for instance that *the rate of internationalization of sales increased by 48 percent in 1996-01 relative to 1990-95* (RELGR value 1.48). That degree of acceleration is more than twice that of production (RELGR for DOIP in Table 7.9 was 1.25). More significantly, that acceleration was attributable to a growth in the rate of extra-regional sales (RELGR 3.62) and not intra-regional sales (RELGR 0.49), which diverges from the patterns in production identified above. The pace of internationalization for intra-regional sales actually *declined* by nearly half in the second period while at the same time extra-regional sales boomed, increasing at a rate over three times as high *after* 1995 as before. The table also shows that extra-regional sales were less and less aimed at the second region, which increased in the second period at only two-thirds of the rate of growth in the first period. Therefore, the *post-1995* period was one of an *acceleration of the rate of intra-regional expansion of production and the extra-regional expansion of sales, and that the extra-regional expansion of sales was not aimed at the second region*.

7.2.4 Network spread and organizational change across the sample

Just as was the case for the internationalization variables, analysis of the subsidiary-based variables includes the values for firms acquired in the period 1995 to 2001. This creates a variable N, which declines from 106 firms in 1990 and 1995 to 89 firms in 2001. That variability is explicitly included because the changing values are intended to reflect the changes in ownership that resulted from the acquisition behavior discussed above. Conceptually, an analysis of only the surviving firms would exclude part of the dynamic. Even so, that dynamic seems minimal given that the effect of including the 16 firms which no longer existed in 2001 is only on the order of one-tenth of a percent difference for the network spread variables in Table 7.12.

Table 7.12: Network spread variables, all companies (1990-2001)

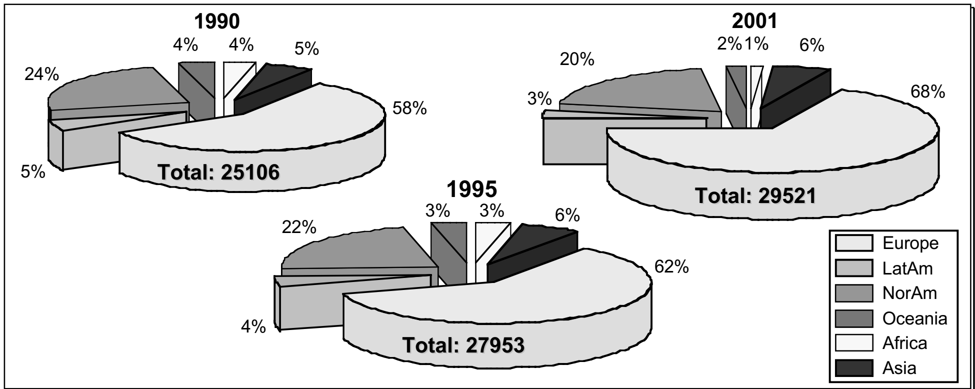
Variables	*1990*[a]	*1995*[a]	*2001*[b]	*Δ1*	*Δ2*
DOISUB	52.6%	52.5%	58.1%	-0.1%	5.6%
HOSTC	26.6	30.6	31.4	14.8%	2.7%
HERF	0.571	0.572	0.602	0.2%	5.3%

a: N=106
b: N=89, excluding the 16 which no longer existed plus Thomson, for which no data were available in 2001

The network spread variables paint a mixed picture. Changes to the overall degree of internationalization in the subsidiary base (DOISUB) and its geographic spread (HERF) occurred primarily in the period 1995-2001, while changes to the number of host countries (HOSTC) took place primarily from 1990-1995. This suggests an incremental network expansion strategy. Since it only takes a single subsidiary in a given country to qualify that country as a ‘host’, an initial expansion with limited subsidiaries into new countries from 1990 to 1995 means an increase in the number of host countries without a noticeable effect on the degree of internationalization and concentration of the network. As the foothold in those new countries is consolidated through expansion of their respective subsidiary bases from 1995 to 2001, the overall degree of internationalization (DOISUB) will rise. In combination with the internationalization data discussed above, these network spread data indicate that *the first half of the 1990s was one of cautious initial internationalization*, while the *second half of the decade involved consolidation and deepening of that internationalization strategy*. The rising concentration index (HERF) means that network expansion was not proportional over the six geographic regions upon which the concentration index is based (Africa, Asia, Europe, Latin America, North America and Oceania). The lower the HERF value, the more dispersed the network is. In this case the HERF value remained unchanged from 1990 to 1995, but increased in the second period, indicating a relatively increased home-region concentration. Together with the rise in the foreign share of subsidiaries and the larger number of host countries, it can be concluded that expansion was primarily *intra-regional* and secondarily *inter-regional*, i.e. first *within* and then *between* North America and Europe.
The prominence of North America and Europe can be seen in Figure 7.2, which shows the aggregate subsidiary base for all companies in the sample in 1990, 1995 and 2001. The

total number of subsidiaries under the companies in the sample increased steadily, from 25,000 in 1990 to 27,000 in 1995 and 29,000 in 2001 (while the number of parent firms declined from 122 to 106 at the same time). On average, therefore, the average core company network increased in size, even without taking into account 'one-off' increases due to acquisitions. While Europe and North America together accounted for 82 percent of the subsidiary base in 1990, by 2001 that share had risen to 88 percent. Latin America, Africa and Oceania declined steadily over the decade, accounting for only six percent of the total base in 2001 compared to nine percent in 1995. Only Asia was able to secure a slight increase, from five to six percent.
Although the North American share of the total subsidiary base declined over the period, due to overall growth the absolute number remained stable, hovering around 6,000 subsidiaries. The number of subsidiaries in Europe grew much more substantially, from 14,500 to 20,000. Since the figures include both host and home subsidiaries, Figure 7.2 shows that the tendency for the average core company from either region is to have more subsidiaries in Europe than in North America. The larger European networks are likely a legacy of macro-Fordism in Europe, which necessitates deeper levels of embeddedness and more complex stakeholder configurations than North American micro-Fordism (see Chapters 3 and 4).

Figure 7.2: Global network spread, aggregate for all firms (1990-2001)



The organizational variables were also most pronounced in the period 1995-2001 (Table 7.13). Evidence of 'downsizing' is not readily apparent in the size of the average core company network over time. The average network grew from 218 majority-controlled subsidiaries in 1990 to 248 in 1995 and again to 308 in 2001. It seem likely that some of the post-1995 increase was due to 'sudden jumps' for a small number of core companies which acquired other core companies. If the nine companies which acquired other core companies are excluded (the 'buyers' discussed above such as Daimler-Benz, BP or Rhône-Poulenc), the averages drop to 204 in 1990, 225 in 1995 and 280 in 2001. This shows that 'buyers' were larger than average. But the growth rates between 1995 and 2001 were identical whether or not 'buying' core companies were excluded, at 24 percent (from 248 to 308 and from 225 to 280, respectively). This indirectly supports the argument made

earlier that the acquisition of another core company does not make a core company eligible for special methodological consideration.

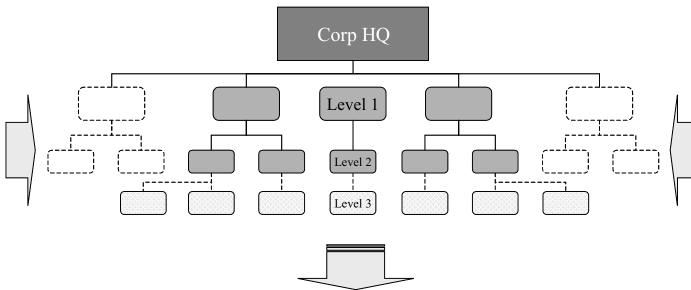
Table 7.13: Organizational variables, all companies (1990-2001)

Variables	*1990*[a]	*1995*[a]	*2001*[b]	*Δ1*	*Δ2*
TOTSUB	218.1	247.7	308.3	13.6%	24.5%
MAXLEV	4.7	4.9	6.0	3.2%	23.5%
PRIM	36.0%	38.2%	24.4%	2.3%	-13.8%
CBL	36.1%	38.0%	30.0%	1.9%	-8.0%

a: N=106; no data for 16 firms
b: N=89, excluding the16 acquired firms plus Thomson, for which no data were available in 2001

As visualized in Figure 7.3, this network growth was primarily one of hierarchical depth, given the increase in maximum level (MXLEV) and decrease in first-level subsidiaries as a share of the whole (PRIM). This deepening involved expansion *within* individual countries as opposed to *across* countries, as evidenced by the declining share of subsidiary relationships extending across borders. The share of cross-border linkages in the subsidiary network shrank from between 35 and 40 percent in 1990-95 (CBL) to 30 percent in 2001. Just as for the network spread variables, the inclusion of the acquired firms in 1990 and 1995 had almost no effect on the average values shown in Table 7.13.

Figure 7.3: Narrowing and deepening of core company networks (1990-2001)



For the sample in its entirety, therefore, all indicators show a tendency towards greater geographic dispersion of production both intra- and extra-regionally. Change after 1995 was significantly greater than change before 1995, and the post-1995 acceleration was primarily intra-regional. To what extent these changes are suggestive of a 'regional integration effect' is best pursued at the level of individual regions and strategies.

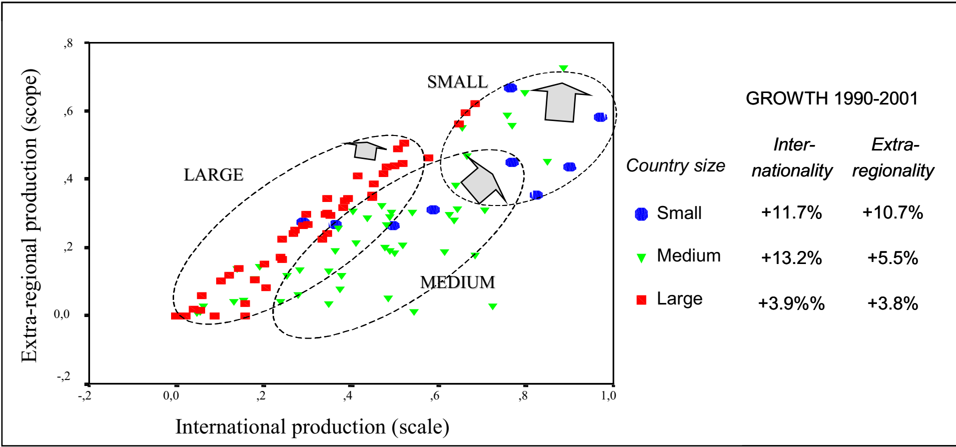
7.2.5 Dynamics by country of origin and sector

In Chapter 6 it was demonstrated that country size was negatively related to internationalization in 1990. Core companies from large countries were the least

international overall as well as the least extra-regional. Core firms from medium-sized countries such as Germany, France and Italy were more international, but still not highly extra-regionally oriented. Only the firms from the smallest countries had on average not only a high degree of overall internationalization, but a high degree of extra-regionality as well. By 2001, as Figure 7.4 shows, all three clusters had become more international and more extra-regional, to varying degrees.

Large-country firms had increased their overall degree of internationalization modestly, from 20.9 percent in 1990 to 24.8 percent in 2001. That increase was also almost entirely extra-regional, perhaps understandable given the small size of the 'host region' for large country firms (i.e., Canada and Mexico). Firms from medium-sized countries had substantially increased their degree of internationalization by 13.2 percent, from 31.7 to 44.9 percent. Just under half of that increase was extra-regional (5.5 percent) with the remainder representing growth within the home region. Small-country firms exhibited the highest increase in internationalization (from 54.6 to 66.3 percent), of which the bulk was extra-regional. Many of the small-country firms, such as Nestlé and ABB, were already highly internationalized in 1990 and thus changed little over the decade. Some of the average change for the subset came in the form of dramatic increases in internationalization of firms like Telefonica and BCE, which in comparison to other small-country firms had very low internationalization levels in 1990.

Figure 7.4: Shifting internationalization by country size (1990-2001)



Thus the overall shifts were greatest for small-country firms such that the gap in internationalization grew over the decade. But when these absolute shifts are compared to the initial degree of internationalization, trends for each country-size subset are much more comparable. For instance, if Company A's DOI share increases from 10 percent in 1990 to 15 percent over 1991-95, the change as a share of the whole is only five percent (15 minus 10 equals 5). In the same way, if Company B's DOI value increases from 50 percent in 1990 to 55 percent in 1991-95, the shift is also five percent. However, in order to compare these shifts, the original (baseline) values must be controlled for. Controlling for the 1990

value generates growth values of 50 percent ([15-10]/10) and ten percent ([55-50]/50) respectively.

In the same vein, the 3.9 percent DOI shift for large-country firms represents one-fifth of the baseline position (20.9 percent), or a growth rate of approximately 20 percent. The 13-percent internationalization shift for firms from medium-sized countries, seen relative to the 1990 degree of internationalization of 34 percent, represents a growth rate of just over one-third. The same calculation for small-country firms (a shift of 11 percent relative to a baseline value of 55 percent) generates a growth rate of 20 percent.

Changes for sectoral clusters can also be analyzed in terms of the difference between percentages in 1990 and 2001 as well as the percentual change relative to the baseline. Table 7.14 shows internationalization changes over time for the eight ‘supersectors’ as defined in Chapter 6: motor vehicles, aerospace and industrial equipment (VEHIC); chemicals and pharmaceuticals (CHEM); computers, electronics and scientific equipment (COMP); food, beverages and tobacco (FOOD); retail and wholesale (RETAIL); petroleum, mining and minerals (PETR); utilities, trading and infrastructure (UTIL) and construction, engineering, forest products and building materials (CONST).

Table 7.14: Internationalization by sector (1990-2001)

	N	DOIP			XRP			DOIP	XRP
		1990	1996-2001	Δ	1990	1996-2001	Δ	Growth	Growth
SERV	17	8.2%	19.8%	11.5%	5.2%	11.0%	5.8%	139.7%	112.6%
RETAIL	22	12.0%	17.8%	5.8%	6.2%	6.2%	0.0%	48.0%	0.2%
VEHIC	20	25.9%	37.5%	11.6%	14.2%	22.2%	7.9%	44.8%	55.5%
CONST	6	34.9%	46.5%	11.6%	22.5%	32.5%	9.9%	33.2%	43.9%
PETR	18	36.4%	45.2%	8.8%	25.6%	32.3%	6.7%	24.1%	26.3%
CHEM	11	42.1%	48.5%	6.4%	31.3%	36.3%	5.0%	15.2%	15.9%
FOOD	12	44.4%	51.1%	6.7%	32.8%	38.2%	5.4%	15.1%	16.4%
COMP	16	44.5%	50.1%	5.6%	30.8%	34.2%	3.5%	12.5%	11.3%

The table shows the degrees of internationalization (DOIP) and extra-regionality (XRP) for 1990 and 2001 plus the ‘delta’ for both variables, which equals the value for 1996-2001 minus the baseline 1990 value. Additionally, the two right-hand columns show the delta as a growth rate by dividing the delta value by the 1990 value to generate a sense of the magnitude of change for different sectors. The table is also sorted in descending order of DOIP growth (second column from the right). The resulting overview shows that sectors which experienced comparable overall shifts, such as UTIL, VEHIC and CONST with DOIP deltas of just over 11 percent, differed considerably in the relative magnitude of that shift. For UTIL companies the 11.5 percent shift represented a more than 100 percent increase in the overall internationalization position, whereas for CONST firms the overall international position increased by a third. At the other end of the spectrum are the most international firms in COMP, FOOD and CHEM, with baseline DOIs of over 40 percent, for which increased internationalization only had a magnitude of 12 to 15 percent relative to the baseline. For these latter firms, changes were therefore less rigorous and invasive and signaled less of a radical departure from preexisting strategy, while UTIL companies,

with traditionally nationally-segmented markets, changed course much more dramatically during the decade. For nearly all sectors, extra-regional expansion was an integral part of increased overall internationalization. RETAIL companies form the only exception in that they essentially did not grow extra-regionally at all, staying at their low 1990 XRP value of just 6.2 percent.

The greater magnitude of change in overall internationalization for the least international companies further indicates a level of *convergence* among internationalization patterns, both overall and in terms of extra-regionality. While in 1990 the most international sector (COMP) was five times more international than the least international sector (UTIL), in the period 1996-2001 that ratio had been cut in half. Similarly, while COMP firms were six times as extra-regional as UTIL firms in 1990, that ratio was also reduced by half in 1996-2001.

Given the relationship between sector and cross-border linkages as a proxy for cross-border integration, it may be that differences in internationalization strategies lead to shifts in the distinction between cross-border integrated firms and multidomestic firms at the level of cross-border linkages. It was already established that on average, the cross-border linkage (CBL) variable declined from just over 35 percent in 1990 and 1995 to 30 percent in 2001. Table 7.15 shows the CBL values for all three years for the integrated (INT) and multidomestic (MDM) firms in the regionally, bi-regionally and globally oriented superclusters.

Table 7.15: Cross-border linkages, integrated versus multidomestic firms (1990-2001)

Variables	*N*	*CBL90*	*CBL95*	*CBL01*
INT	47	44.2%	44.6%	36.2%
MDM	16	35.7%	43.4%	30.2%

N=63 (excludes DOM through DOM+ and firms missing data for one or more years)

The table shows that integrated firms remained unchanged in their cross-border linkages from 1990 to 1995 before declining sharply by 2001. Multidomestic firms posted a significant initial increase in cross-border linkages from 1990 to 1995 before declining again even more sharply by 2001. The difference may be explained in two stages. First, it has been established that the first half of the 1990s was used primarily for initial, relatively shallow expansion into new countries. The stable CBL value for integrated firms means this expansion was conducted equally within countries and across countries (every other new subsidiary is across a border from its immediate parent). The jump in CBL for multidomestic firms, on the other hand, means that growth in the subsidiary base occurred by subsidiaries acquiring or establishing subsidiaries in other countries as opposed to establishing deeper networks within those countries. After 1995, both types consolidated their respective networks by expanding *within* individual national structures. Although INT firms continue to exhibit higher levels of cross-border linkages inherent to their cross-border character, the evidence suggests MDM firms attempted to consolidate their activities at a higher level than the national one, pointing again towards a degree of strategic convergence.

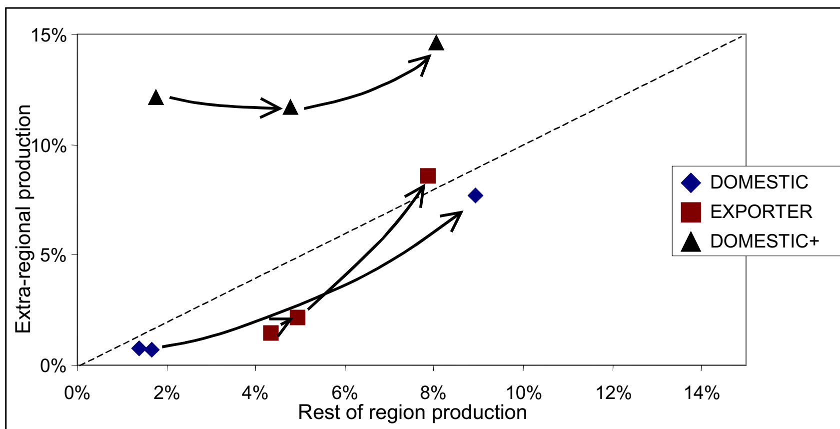
7.3 European core company strategies

In the following sections the strategy clusters of European core companies will be discussed in terms of changes to their key features over time; i.e., their strategy migrations (cf. Chapter 4). For the sake of comparison, and to keep the analysis of 12 separate clusters manageable, the strategy clusters will be addressed on the basis of the four overarching categories: domestically oriented companies (DOM, EXP and DOM+); regionally oriented companies (RDL, RMDM, RDL+ and RMDM+); bi-regionally oriented companies (BiRDL, BiRMDM, BiRDL+) and globally oriented companies (GLOB and GLMDM). To establish a solid reference point, firms will continue to be identified and clustered by their 1990 baseline strategy classification even as their strategies change over time. At the end of the section firms will be 'reclassified' on the basis of the same general parameters used in 1990 in order to qualify the nature of the strategy migrations.

7.3.1 European domestically-oriented companies

The three clusters of domestically-oriented core companies (DOM, EXP and DOM+) began the decade with internationalization values (DOIP) of 2.2, 5.8 and 13.9 percent, respectively. Of these modest values, more than half for both DOM and EXP firms was inside Europe. DOM+ firms were by definition primarily active outside the home region, as for example the British supermarket chain Sainsbury, whose limited international activity was solely in North America. Fundamentally, the question for domestically oriented firms is to what degree they internationalized over the two periods, and whether that internationalization had a primarily intra- or extra-regional character. For this reason the axes used thus far (internationalization and extra-regionality) are replaced in Figure 7.5 with intra-regionality and extra-regionality.

Figure 7.5: Internationalization, European domestically-oriented core companies (1990-2001)



The arrows between the data points in Figure 7.5 represent the strategic migrations over 1991-95 and 1996-01. For all three clusters, the figure shows a clear pattern of

internationalization, whereby in particular for DOM and EXP firms the main thrust took place after 1995. The dotted diagonal shows the line along which internationalization is evenly spread between intra- and extra-regional shifts. Both DOM and EXP companies followed this line to some extent, although two of the three exporters in fact show an increasing tendency to seek expansion outside the home region. As argued in Chapter 4, exporters are most likely to be impacted by reductions in regional tariff structures and thus the need for tariff-jumping regional internationalization is reduced. This supposition, which remains anecdotal given the small sample size, is supported by changes in the internationalization of sales relative to production (Table 7.16)

Table 7.16: Changing sales-to-production ratios for European exporters (1990-2001)

	DOIP			*DOIS*			*Ratio S/P*		
	90	1991-95	1996-01	90	1991-95	1996-01	90	1991-95	1996-01
Veba	5.0%	8.9%	25.3%	28.8%	27.8%	41.1%	5.8	3.1	1.6
IRI	4.5%	4.5%	6.0%	18.4%	19.6%	35.0%	4.1	4.3	5.8
RAG	7.9%	7.8%	18.0%	12.9%	12.8%	23.0%	1.6	1.6	1.3

Both Veba and RAG followed an extra-regional internationalization pattern over the 1990s, which, *ceteris paribus*, was more likely to face barriers to trade than intra-regional internationalization in the wake of the Single European Market. Hence, the ratio of foreign sales to foreign production declined as production, in relative terms, internationalized more quickly than sales. For IRI, on the other hand, whose strategy was primarily aimed at Europe, internationalization over the 1990s has resulted in an intensification of the export-based strategy.

The nine domestic companies, which were uniformly stable in the first half of the decade, showed a more dispersed pattern after 1995, with some developing an explicit regional orientation (e.g., Metro, RWE, France Telecom, British Telecom and Tesco) while in particular Telefonica focused primarily on extra-regional expansion into Latin America, increasing its XRP value from virtually nil in 1990 to 27 percent in 2001. DOM+ companies, on the other hand, may have seen their core positions threatened by more regionally oriented competitors in a regionalizing world. All three (Sainsbury, Lufthansa and ENI) shifted proactively towards a more solid regional base in the run-up to the Single Market before steering into a more balanced internationalization pattern after 1995.

The network spread variables substantiate the location shifts identified in the strategy data. Table 7.17 shows how the foreign share of the subsidiary base grew rapidly over the second period, as well as the number of countries. For the three exporters, the number of countries in which they have subsidiaries first rose in 1995 in combination with a higher Herfindahl index (HERF), suggesting that internationalization of the subsidiary base was primarily intra-regional. By 2001, however, the number of host countries had declined and the HERF value dropped slightly, indicating some degree of intra-regional rationalization.

Domestic companies increased their degree of internationalization and the number of host countries fairly radically, but this did not lead to a significant increase in the overall degree of dispersion (i.e., a lower HERF index). This supports the evidence above that most DOM companies focused their internationalization strategies on the home region. Similarly, DOM+ companies increased the number of host countries significantly after 1995 but

maintained a fairly stable geographic spread, confirming the notion that such firms shifted their orientation from highly extra-regional to a greater extra- and intra-regional balance.

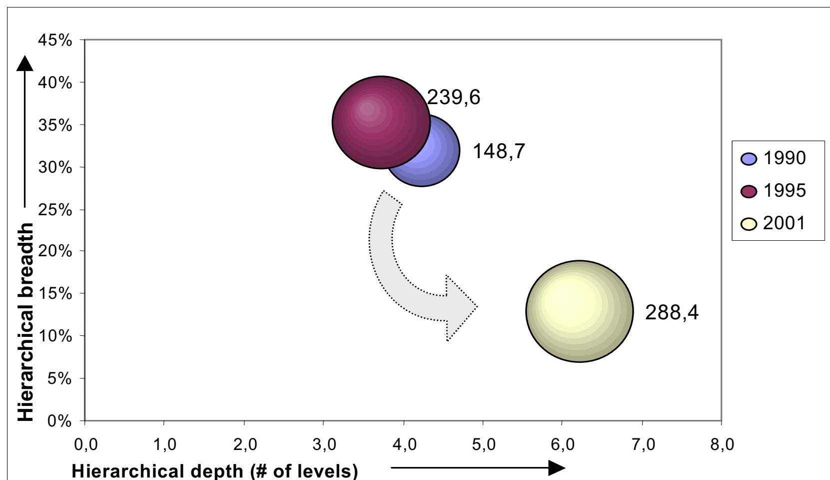
Table 7.17: Network spread, European domestically oriented strategies (1990-2001)

		DOISUB			*HOSTC*			*HERF*		
	N	90	95	01	90	95	01	90	95	01
DOM	9	19.0%	26.8%	44.9%	4.9	9.1	18.8	0.834	0.827	0.781
EXP	3	26.2%	28.4%	39.0%	20.7	29.3	23.0	0.807	0.839	0.799
DOM+	2[a]	40.8%	37.7%	58.1%	20.0	21.0	29.5	0.660	0.640	0.654

a: excludes Sainsbury, for which no subsidiary data was available in 1990

In terms of their organizational structure, all three domestically oriented strategy types followed identical patterns and thus the three can be clustered for manageability. Figure 7.6 shows the size of the overall subsidiary base (indicated by the size of the bubbles), the breadth of the network, measured by the share of first-level subsidiaries in the total and the hierarchical depth of the network, measured by the number of levels in the ‘corporate tree’.

Figure 7.6: Organizational structure, European domestically-oriented core companies (1990-2001)



All three domestically oriented clusters grew in average network size from 1990 to 1995 and again to 2001. At the same time they all experienced a slight reduction in depth and a corresponding increase in organizational breadth from 1990 to 1995, before becoming considerably narrower and deeper in the second period. Since the first period was also characterized by one of limited network spread, it is possible that organizational reconfiguration at that time involved a (vertical) consolidation of activities involving the elimination of domestic complexities in preparation for international expansion from 1995 to 2001. The latter expansion apparently involved not only an expansion into new

countries (see Table 7.17), but therefore also an extensive deepening of network penetration in existing host countries.

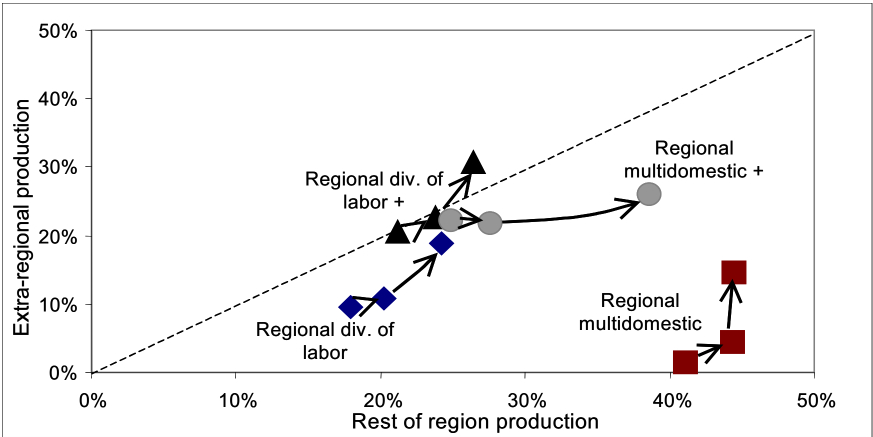
7.3.2 European regionally-oriented companies

The four regionally-oriented clusters of firms together comprise the largest group of the European core companies in the sample (N=33), and hence their strategic migrations have a proportionately large impact on the sample as a whole. Hence, the trends in intra- versus extra-regional growth (Figure 7.7) do not come unexpected. At the same time, the averages used to plot the figure represent a great number of firms with mildly heterogeneous strategic migrations and is therefore best seen as purely indicative. That heterogeneity will be addressed with specific examples as needed.

As shown in Figure 7.7, integrated European core companies (RDL and RDL+) followed nearly identical paths over the decade. In both cases they expanded slightly more extra-regionally than intra-regionally, and in both cases that expansion was more significant after 1995. Multidomestic strategies (RMDM and RMDM+), however, appeared to converge within an intensified *intra*-regional focus.

Firms within clusters do exhibit a considerable degree of diversity, particularly among the integrated firms (RDL and RDL+). Some firms, like BMW, expanded intra-regionally in 1991-95 (with the Rover acquisition in 1994). Renault expanded within Europe over both periods, but its expansion was largely in Eastern and Central Europe. Others even contracted slightly, such as Peugeot, Usinor, Total and Siemens, before expanding in the region more dramatically in 1996-01. In fact, three RDL companies ended the decade with a smaller regional share than they began with (Usinor, Ericsson and Alcatel).

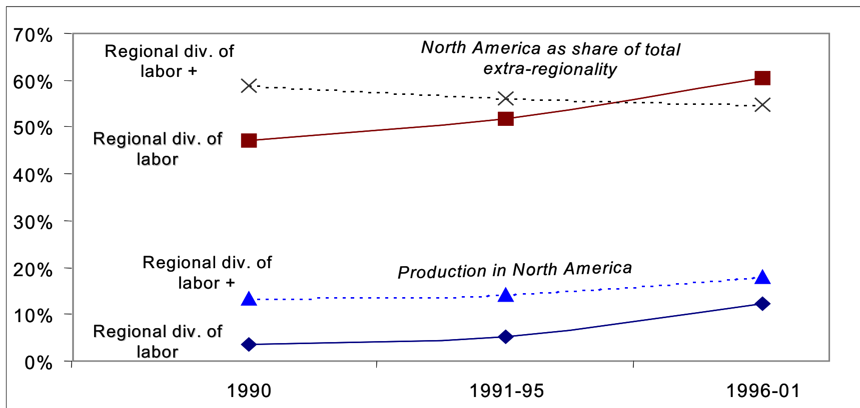
Figure 7.7: Internationalization, European regionally oriented core companies (1990-2001)



Nearly all RDL firms expanded extra-regionally over the decade, and in all cases expansion was significantly greater after 1995. In 1990, the 11 RDL companies had an extra-regional share of production of 9.5 percent, rising slightly to 10.7 percent in 1991-95 before climbing to 18.9 percent in 1996-01. RDL+ firms were on average more likely to

expand aggressively outside the region. In some cases (e.g. Total and Daimler), this also contributed to a reduction in the share of activity in the home region (due to acquisitions of Petrofina / Elf Acquitaine and Chrysler, respectively).
The four RMDM+ firms (Ferruzzi, Carrefour, Gen. des Eaux and Suez Lyonnais des Eaux) were also not entirely consistent in their internationalization patterns. Gen. des Eaux and Carrefour, on the other hand, moved upward and to the right along the diagonal in Figure 7.7 while Suez and Ferruzzi expanded aggressively within Europe. The path identified for the two RMDM firms (Promodes and Danone) on the other hand in reality reflects the strategy of Danone. Danone pursued an aggressive extra-regional acquisition strategy in Asia and to some extent in the Americas in the second half of the 1990s, while Promodes was relatively stable (before being acquired by Carrefour in 1998). The greater degree of diversity of multidomestic strategies relative to integrated strategies may very well be a reflection of the diverse 'local responsiveness' pressures experienced by the former.
Shifts in regional activity were in most cases related to shifts in extra-regional activity and the role of North America as the 'second' region. In general, both RDL and RDL+ companies expanded activity in North America, but the North American share as a percentage of total extra-regional activity *declined* for RDL+ companies while it increased for RDL companies (Figure 7.8). This suggests that RDL firms were also developing a regionally organized strategy in North America, in effect transplanting their home region strategy (and possibly even growing in the direction of a BiRDL strategy), while RDL+ firms were exporting the 'extra-regional' characteristics of their existing strategy to the rest of the world (Daimler, however, clearly opted for a BiRDL strategy through its acquisition of Chrysler).

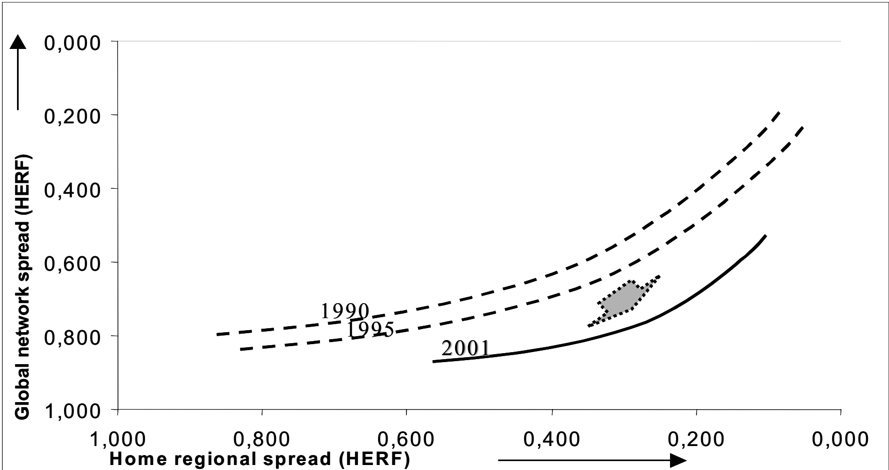
Figure 7.8: Expansion into North America, European regionally oriented core companies (1990-2001)



In theory, regionally organized companies can be expected to experience major network spread effects in the wake of integration, in the form of reduced geographic spread (concentration) or, as discussed in Chapter 4, increased geographic spread (dispersion). To explore the regional aspects of network spread effects, variables were adapted to the home region context. Firstly, a Herfindahl index of concentration was developed for the subsidiary base in only the EU15 (plus Switzerland, since ABB, an RDL+ firm, is both

Swiss and Swedish). Again, the lower the index value, the more evenly dispersed the subsidiary base is. The regional Herfindahl spread is compared with the overall global Herfindahl spread for all four regionally-oriented strategy clusters in 1990, 1995 and 2001 in Figure 7.9 (the two dimensions are independent because global spread is measured by aggregating subsidiary bases at the regional level; spread *within* the region is immaterial).

Figure 7.9: Intra-regional network spread, European regionally oriented core companies (1990-2001)



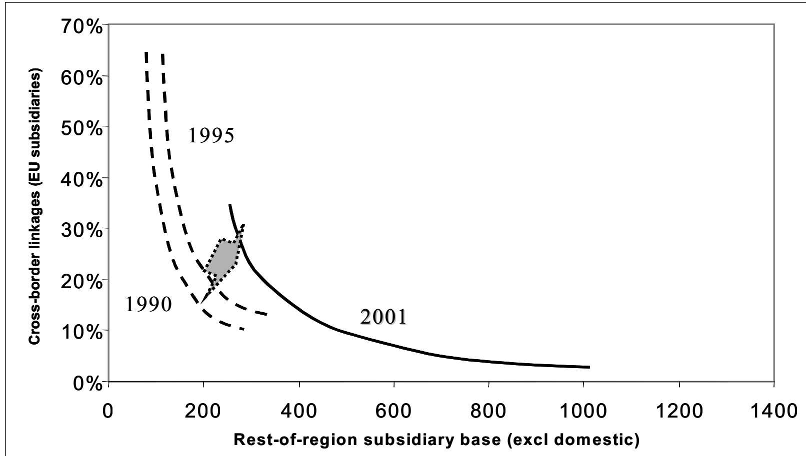
N=27; for 6 firms subsidiary data were not available for all three years

The general dispersion for each year is represented by the three dotted curves designated 1990, 1995 and 2001 respectively in Figure 7.9. Over time, the curve makes a clear push to the right, indicating an *increased* degree of dispersion within the home region in the course of the 1990s. At the same time, the curve shifts *downward*, indicating that regionally oriented firms are more concentrated globally. Combined the trend shows that regionally oriented firms are becoming increasingly regional both in terms of a declining extra-regional network spread as well as in terms of increased intra-regional penetration. Moreover, the curve becomes shorter, signaling a reduced bandwidth, or smaller deviation from the mean, over time. The tendency is therefore once again one of convergence.

The focus on shifts specifically within the home region can be linked to organizational matters as well. The data show that the aforementioned intra-regional penetration was accompanied by a parallel expansion of the subsidiary base in European *host* countries, i.e. excluding domestic subsidiaries (Figure 7.10), which for regionally oriented companies on average increased from 186 in 1990 to 211 in 1995, before climbing to 345 in 2001. The increase in network size occurred in conjunction with a reduction in the overall share of cross-border linkages among subsidiaries in the European Union. Those linkages were measured using cross-border linkage data for the EU alone (EU_CBL), which measures the likelihood that any given subsidiary in any of the EU15 countries has a parent in another EU15 country. EU_CBL rose slightly from 30 percent in 1990 to 33 percent in 1995 before dropping to below 22 percent in 2001. This indicates that post-1995 intra-regional network expansion was primarily one of deepening existing networks within individual European

Union countries: new subsidiaries were acquired or founded under existing subsidiaries in the same country, and not across borders.

Figure 7.10: Intra-regional organization, European regionally oriented core companies (1990-2001)

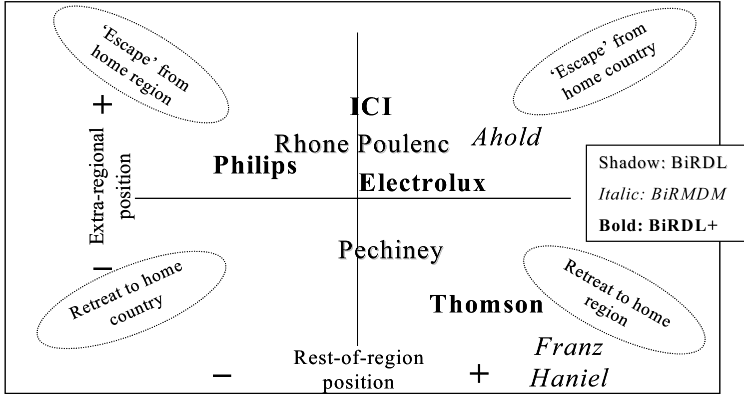


N=27; for 6 firms no subsidiary data were available for all three years

7.3.3 European bi-regionally-oriented companies

The bi-regionally oriented cluster of strategy types (BiRDL, BiRMDM and BiRDL+) is considerably smaller than the regionally oriented cluster, consisting of eight firms. These eight firms, however, show a greater variety of strategy migrations. The average values per subtype are of limited value because in fact they tend to cancel out opposing trends. As a result the general trends in terms of intra- and extra-regional shifts are given indicatively in Figure 7.11. Instead of reflecting variable values over 1991-95 and 1996-01 averaged by strategy types, Figure 7.11 shows the strategy migrations of all 8 companies in terms of changes to rest-of-region and extra-regional production over the period as a whole. The figure represents four quadrants in which production shares over each axis either increased or decreased. The changes, as for the entire sample, occurred primarily from 1996 to 2001. In essence four combinations are possible. If the rest-of-region share of activity declines in combination with a decline in extra-regional activity, this by definition implies a relative shift towards the home market (bottom left). If the share of activity in the home region increases and the extra-regional share decreases, the firm has in relative terms retreated to the home region. The most dramatic example of such a shift is Franz Haniel, which in 1990 had a fairly even split between its home country, Germany, and the United States as the basis of its BiRMDM classification. By 2001 Franz Haniel's activities in the US had been reduced to three percent of the total and 69 percent was located in (non-domestic) Europe. These represent relative shifts in terms of the total, not absolute contractions: Franz Haniel was still more *international* in 200 than in 1990 (overall degree of internationalization was 77 percent compared to ca. 50 percent), but dramatically less extra- (and thus bi-) regional.

Figure 7.11: Internationalization, European bi-regionally oriented core companies (1990-2001)



The upper left quadrant reflects a strategy by which the home region was reduced in its overall share of activity while extra-regional activity increased. Philips is the only company that fell in this category, reducing its rest-of-region activity from over 40 to under 32 percent over the decade while increasing the extra-regional share from 37 to 45 percent (related to its sale of the Polygram media division to Seagram's in 1998). The upper right quadrant represents a strategy by which both the rest-of-region share and the extra-regional share increase at the expense of the home country. Ahold is the clearest example of such a trend, having expanded its activities in both Europe and the Americas in the second half of the 1990s.

The 'escape from home country' strategy may or may not entail a 'fortification' of the bi-regional strategy. That is, the extra-regional expansion may not necessarily be concentrated in the second region. This can be seen in the figures for the second region (North America) for bi-regional firms. Table 7.18 shows the share of total activity in North America and North America as a percentage of overall extra-regionality for seven of the eight companies. The table shows that four companies (in bold type) had shifted activity towards North America in relative terms (as a share of total activity) over the decade, while North America declined in relative importance for the other three.

Table 7.18: Expansion into North America, European bi-regionally oriented strategies (1990-2001)

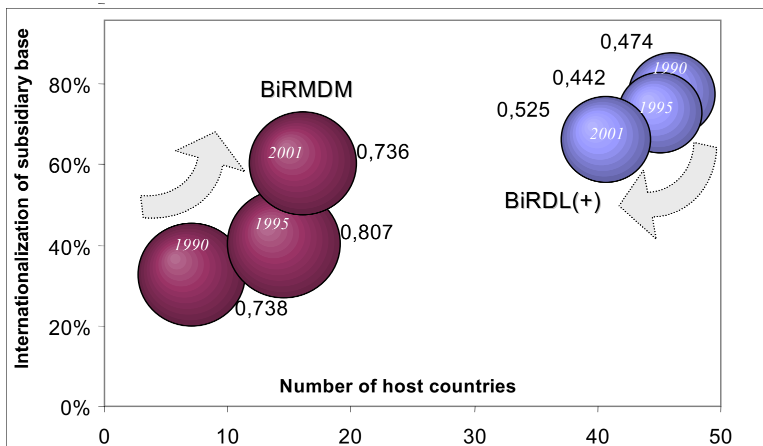
		Activity in North America			*As % of total extra-regionality*		
	STRAT	1990	1991-95	1996-01	1990	1991-95	1996-01
Rhône-Poulenc	BiRDL	32.9%	31.5%	37.1%	81.8%	78.4%	78.9%
Pechiney	BiRDL	37.0%	32.8%	21.8%	92.5%	89.3%	75.0%
Ahold	BiRMDM	52.8%	55.8%	51.1%	100.0%	100.0%	76.7%
Franz Haniel	BiRMDM	55.0%	36.9%	3.0%	100.0%	100.0%	100.0%
Philips Electronics	BiRDL+	13.0%	12.0%	14.4%	35.1%	29.2%	32.1%
Electrolux	BiRDL+	21.7%	23.6%	24.1%	50.8%	56.0%	55.2%
ICI	BiRDL+	23.4%	24.9%	37.1%	59.5%	48.6%	63.0%

N=7 (Thomson data unavailable)

The shift towards North America, however, does not necessarily represent a narrowing of a company's extra-regional strategy. In fact, for only two of the eight bi-regional companies (ICI and Electrolux) did North America account for a larger share of its *overall* extra-regional activity in 2001 than in 1990. Ahold, on the other hand, grew absolutely in the United States in the 1990s while at the same time expanding in South America through its acquisitions in Brazil and Chile. As a result its RG2P value dropped only slightly over the decade, from 52 to 50 percent, but while that RG2P value in 1990 represented 100 percent of Ahold's extra-regional activity, by 2001 it only accounted for 76 percent.

The fairly rigorous shifts either out of the home region or out of the second region suggest that the bi-regional strategy may have become less viable after 1995. Firms either tried to move in the direction of global or retreated back to more of a regional emphasis in an attempt to adapt to changing priorities. These developments may also be evident in the network spread variables. Figure 7.12 shows the average changes in the foreign percentage of the subsidiary base, the number of host countries and the Herfindahl concentration index (beside the bubbles) for the BiRDL(+) and BiRMDM strategy types.

Figure 7.12: Network spread, European bi-regionally oriented core companies (1990-2001)



The BiRDL and BiRDL+ firms are combined here because the values for these variables are not materially different (the difference is in the degree of involvement in countries outside the EU and North America, i.e. the *size* of the subsidiaries, not their absolute numbers). The figure shows that the two multidomestic firms, Ahold and Franz Haniel, grew both in terms of degree of internationalization and number of host countries. These migrations can be qualified by the internationalization variables above, which already showed that in the case of Franz Haniel the change was primarily a shift back to Europe, whereas for Ahold it involved an expansion strategy in Europe, North and South America. Both strategies produced a relatively stable overall subsidiary concentration over time.

The cross-border integrated firms, on the other hand, showed on average the opposite trend. The number of host countries declined as did the overall degree of internationalization of the subsidiary base (the major exception was Rhône-Poulenc, which

was considerably larger in 2001 than in 1995, due to its acquisition of Hoechst in 1999). Moreover, after declining slightly from 1990 to 1995, the Herfindahl index rose in 2001. The declining number of host countries shows that this increased overall concentration of the subsidiary base involved not only a shift towards a limited number of regions, but also away from some countries. Philips, for instance, had majority-controlled subsidiaries in 69 countries as of 1995 but in only 45 countries in 2001. This reduction was largely at the expense of Sub-Saharan African countries and other less-developed countries, while the subsidiary base in developed countries increased.

These trends among integrated firms are all the more striking when compared to the average network shifts over the entire sample which show an increase in both the number of host countries and the overall degree of internationalization. Thus integrated bi-regional strategies exhibit a radical departure from the overall trend, which reinforces the conclusion that these strategies were less and less viable in a regionalizing world. The evidence has shown this to be less of a factor for the multidomestic strategy, reiterating once again how regionalism has a different significance for integrated production versus local responsiveness. The apparent convergence between integrated and multidomestic patterns underscores the trends identified for the sample as a whole.

Bi-regional firms also experienced some degree of convergence in terms of organizational structures (Table 7.19). Both types of networks showed a gradual deepening of their hierarchies accompanied by a reduction in the share of first-level subsidiaries (hierarchical breadth). The latter change was particularly dramatic for BiRMDM firms, which were very broad and shallow in 1990, then experienced moderate deepening in 1995 before transforming their structures to a deep and narrow pyramid in 2001. Cross-border linkages followed the same pattern as for regionally oriented strategies, rising first from 1990 to 1995 before falling below the 1990 level in 2001.

Table 7.19: Organizational structure, European bi-regionally oriented strategies (1990-2001)

	BiRDL(+)			BiRMDM		
	1990	*1995*	*2001*	*1990*	*1995*	*2001*
TOTSUB	390	324	260	158	200	395
PRIM	26%	30%	25%	48%	48%	9%
MXLEV	5,80	6,40	6,40	3,50	4,50	7,00
CBL	41%	44%	36%	23%	30%	12%

The table also shows that overall network size developed in opposite directions, with BiRDL firms becoming significantly more streamlined over time and BiRMDM firms considerably larger such that the two virtually reversed positions. In 1990, BiRDL firms had networks consisting on average of 390 subsidiaries, which dropped steadily to 260 in 2001, while BiRMDM firms grew from 158 in 1990 to 395 in 2001.

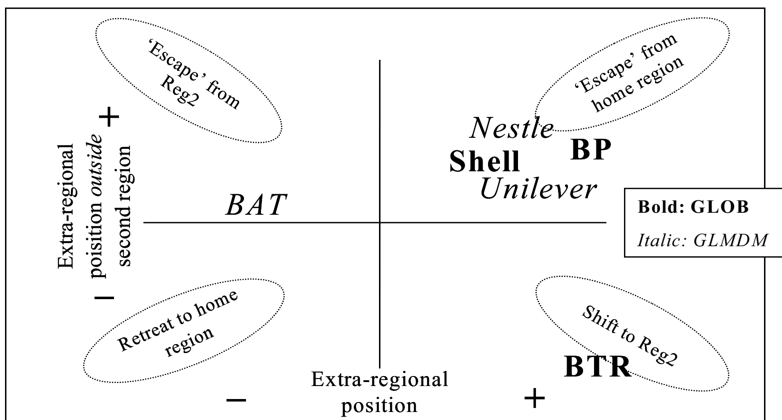
7.3.4 European globally-oriented companies

The greater a company's scale and scope, the more room there is in which to maneuver and thus the more facets of strategy are subject to change. Europe was home to only six globally oriented companies in 1990, three of which based on a cross-border integrated

production strategy (GLOB) and three of which based on a multidomestic strategy (GLMDM), yet the six show some degree of variation in a number of the key variables. Given the scale of the globally oriented strategy, the focus in the analysis is on trends in extra-regional activity and the role of North America (as the second region) versus the rest of the world. Overall internationalization is of lesser importance, not only for the analysis but also strategically to the firms as well, since two of the six (Unilever and Shell) do not even specify 'domestic' activity, referring to 'European' activity instead.

Figure 7.13 shows the main thrusts of internationalization for all six firms based on a horizontal axis of increasing extra-regional production and a vertical axis of *decreasing* second-region shares of extra-regional activity, i.e. a higher 'rest of world' share of activity. As in Figure 7.11, the two axes represent four quadrants, in which the upper right signifies an expansion strategy based on relative shifts outside both Europe and North America, or a deepening of the 'global' character of the firm's strategy, and the lower left signifies a retreat into both Europe and North America, which in effect would constitute a bi-regional strategy. The upper left quadrant represents a relative retreat from North America back into Europe while the lower right quadrant represents a relative shift from Europe to North America.

Figure 7.13: Extra-regional internationalization, European globally-oriented companies (1990-2001)



Nestlé, Shell, Unilever and British Petroleum fall into the upper right quadrant, indicating they all continued to reinforce their existing global strategies during the 1990s by expanding not only outside of Europe, but outside of North America as well. In fact, North America declined not only as a share of extra-regional activity, but as a share of total activity. BP, whose North American share of total activity did increase from 1995 to 2001 through its acquisitions of Amoco and Atlantic Richfield, was the only exception: North America accounted for only 64 percent of its extra-regional activity in 2001 (69 percent in 1990), but North America as a share of BP's total activity increased from 32 percent in 1990 to 36 percent in 2001. BTR, on the other hand, continued to pursue an extra-regional expansion strategy in which North America increased not only as a share of the total but

also in its relative importance as the central component of its extra-regional orientation. BAT's strategic migration was the most unique, representing not only a partial retreat into Europe (including the tobacco fields of Eastern Europe) but also a slight shift away from North America through aggressive acquisitions in South America.

Although Figure 7.13 creates the impression that regional activity declined over the period, the data in Table 7.20 show that extra-regional expansion occurred primarily at the expense of domestic activity, and much less so at the expense of the rest of the home region. Table 7.20 shows the DOIP and RORP values for the four companies reporting domestic activity (recall that Shell and Unilever report 'Europe' only). The table shows that three of the four (BP, BTR and Nestlé) became more international over the decade. BAT, which in 1990 had the highest extra-regional value of all companies in the sample, became in fact less international over the decade. Only BTR expanded its rest-of-region share noticeably, from 10.5 percent in 1990 to 15.7 percent in 2001.

Table 7.20: Intra-regional internationalization, globally oriented strategies (1990-2001)

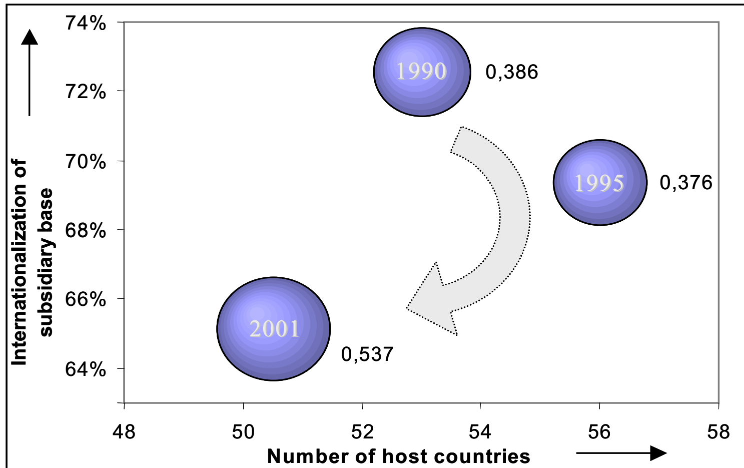
		International production (DOI)			*Rest of region production (ROR)*		
		1990	*1991-95*	*1996-01*	*1990*	*1991-95*	*1996-01*
BP	GLOB	73.9%	73.0%	76.7%	26.7%	26.7%	20.8%
BTR	GLOB	75.7%	79.8%	88.4%	10.5%	10.6%	15.7%
Nestlé	GLMDM	96.5%	96.8%	97.2%	42.0%	42.6%	39.1%
BAT	GLMDM	86.1%	87.1%	79.6%	14.9%	15.1%	14.2%
	Avg	**83.1%**	**84.2%**	**85.5%**	**23.5%**	**23.7%**	**22.4%**

The overrepresentation of British companies in this cluster seems to have had considerable impact on the outcomes. British companies have traditionally leaned towards North America in their orientation, a factor which has no doubt contributed to the relatively ambivalent attitude of British politicians as well as companies towards the European Union. It appears that British companies were anything but unanimous in their strategic decisionmaking with regards to spatial restructuring in a regionalizing world. Some, like Shell, Unilever opted for an absolute extra-regional focus, looking beyond both Europe and North America, while BTR expanded into Continental Europe in conjunction with solidifying its base in North America. At the same time BP's strategy, through its acquisition of Amoco and ARCO, took on more of a bi-regional character and BAT retreated in relative terms from both regions. This diversity (also the lack of a clear distinction between GLOB and GLMDM) suggests that regionalism, however important, was less critical for globally-oriented firms than for those centered on one or two regions.

The relatively slight increase in internationalization runs counter to developments in the network spread of globally oriented firms. Figure 7.14 shows the degree of internationalization of the subsidiary base, the number of host countries and the Herfindahl concentration index for the four globally-oriented companies for which data were available (BAT, Nestlé, BTR and BP). The internationalization of production combined with a relative *de-internationalization* of the subsidiary base suggests that foreign production was being rationalized and consolidated, or possibly that diversity in the product portfolio was being reduced. This is also reflected in the decline in host countries over the decade as a whole, and the increase in the degree of concentration. The fact that the rise in HOSTC

from 1990 to 1995 had little impact on the concentration index shows that the additional countries did not represent any large-scale expansions, whereas the shift from 1995 to 2001 was clearly more substantial.

Figure 7.14: Extra-regional internationalization, European globally-oriented companies (1990-2001)



These developments are also reflected in the organizational structure of globally-oriented firms (Table 7.21). Their average subsidiary base contracted over the decade from an average of 659 in 1990 to 537 in 2001, parallel to the reduction in the degree of internationalization of the subsidiary base, indicating that network contraction was primarily aimed at foreign subsidiaries. The contraction of the network base affected not only the breadth, but also the depth of the globally oriented organization. The share of first-level subsidiaries dropped from over 20 percent in 1990 to just over ten percent in 2001, while maximum depth declined from 8.3 levels to 7.5. The overall decline in the share of cross-border linkages over the decade is in all likelihood related to the decline in the number of host countries and de-internationalization of the subsidiary base.

Table 7.21: Organizational structure, European globally oriented strategies (1990-2001)

	1990	*1995*	*2001*
TOTSUB	659	586	537
PRIM	21.6%	25.0%	10.9%
MXLEV	8.3	7.8	7.5
CBL	37.8%	40.7%	27.7%

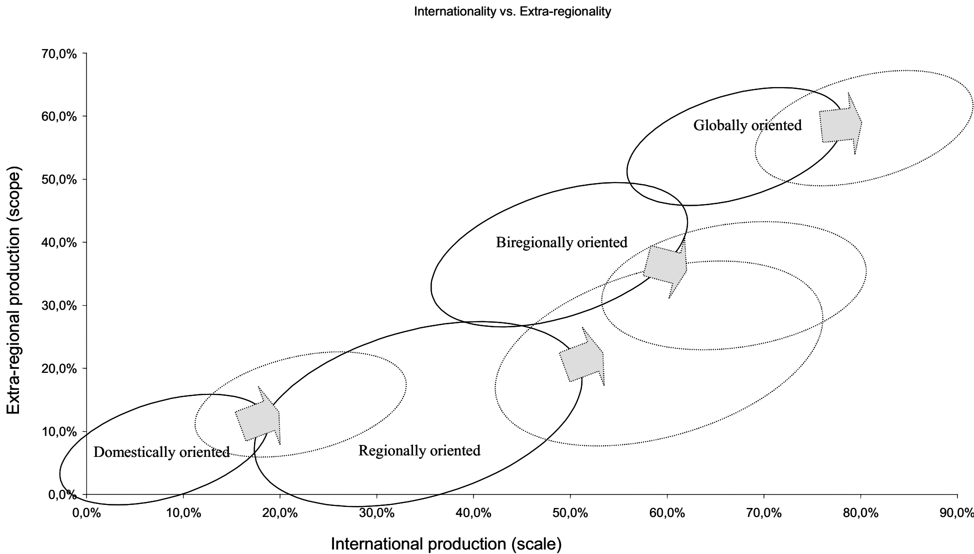
7.3.5 Interim conclusions, pt. 1

The more international and extra-regional a firm is, the more difficult it becomes to pinpoint trends. This is not only obvious from a methodological and managerial point of

view (there are more variables or 'levers' of strategy to manipulate), but also from a theoretical point of view. Globally oriented companies, for instance, are simply exposed to a far greater range of stakeholders, competitive pressures and other strategic considerations than e.g. a domestic company. Given that the scope of globally oriented companies extends well beyond the competitive space of integrating Europe, regionalism can generally be expected to be less of a strategic issue. Moreover, in terms of total activity, global companies are by definition the least European and thus any 'integration effect' will be less apparent at the level of overall geographic dispersion of activity. Yet precisely these firms (e.g. Nestlé, Shell) were such outspoken advocates of integration. Conversely, domestic and regionally-oriented companies had a much clearer stake in European integration in terms of its spatial implications.

Whereas the overarching trend across all clusters over the decade was towards more internationalization, both extra-regional and intra-regional, European core company internationalization strategies have shown varying degrees of divergence. Bi-regionally oriented company strategies were the most striking in their departure from the norm, suggesting that a bi-regional focus became less viable, particularly after 1995. Note the exception of Philips, which, as one of the 'founding fathers' of the single market idea, was the only of the bi-regionally oriented firms to pursue a strategy tantamount to 'escaping the home region'. Figure 7.15 shows the migrations by main clusters of strategy types along the two key dimensions identified in Chapter 6 (extra-regionality and overall internationality), and underscores the observation that by 2001, the bi-regional cluster had largely converged with the regionally oriented cluster. At the same time the domestically oriented cluster had moved into the position previously occupied by the regionally oriented cluster; hence for all strategy types except GLOB and GLMDM, the significance of Europe in European core company spatial strategies had increased profoundly.

Figure 7.15: Strategy migrations, European companies (1990-2001)



In the current analysis, the baseline typology classification was maintained in order to follow changes in a structured fashion. However, the changes to the strategy variables over time alters the very foundation of the classification itself and thus classification into the predefined strategy clusters based on the 2001 values would likely lead to a very different clustering. Table 7.22 shows the changing cluster sizes based on reclassification between 1990 and 2001.

Table 7.22: Reclassification of European strategy types based on average values 1996-2001

STRAT	N (1990)	N (2001)	XRP (1990)	XRP (1996-01)	DOIP (1990)	DOIP (1996-01)
DOM	9	3	0.8%	0.7%	2.2%	3.3%
EXP	3	1	1.5%	3.0%	5.8%	6.0%
DOM+	3	2	12.2%	12.4%	13.9%	15.8%
RDL	11	5	7.3%	5.6%	24.4%	30.6%
RMDM	2	3	1.6%	3.5%	42.6%	40.1%
RDL+	16	20	22.4%	21.5%	44.2%	40.8%
RMDM+	4	5	22.3%	26.4%	47.1%	64.3%
BiRDL	2	6	40.1%	37.8%	57.7%	62.8%
BiRMDM	2	0	53.9%	.	56.4%	.
BiRDL+	4	4	40.0%	41.5%	65.7%	74.7%
BiRMDM+	0	1	.	66.6%	.	76.5%
GLOB	3	4	56.2%	62.5%	74.8%	80.2%
GLMDM	3	3	62.9%	61.8%	91.3%	88.4%
Total	**62**	**57**	**19.3%**	**25.3%**	**35.6%**	**47.6%**

Since five firms were acquired by 2001 the overall N decreased from 62 to 57. The cluster of domestically oriented strategies was reduced from 15 firms to six, primarily at the expense of the absolutely domestic firms (from nine to three). The regionally-oriented cluster remains steady at 33 firms, but within the cluster there was a clear shift from RDL to RDL+ strategies (11 to 5 and 16 to 20, respectively). There were 11 bi-regionally oriented companies in 2001 compared to eight in 1990, but again the parameters for this cluster in particular were markedly different in 2001, involving a higher DOIP value and RORP value, lower XRP value and a lower concentration of extra-regional activity in XR2. In other words the bi-regional strategy as it existed in 1990 did not appear successful as an internationalization strategy, but through the enhanced emphasis on the home region in 2001 (and reduced dependence on the second region) may emerge as viable in the future. The globally oriented cluster was the most stable over the decade (but at higher overall variable values), with only one formerly bi-regional firm migrating to a GLOB strategy. *Thus regionalism may create a 'chasm' between the regional and the global which bi-regional firms are forced to straddle. Bi-regional firms which do not gain sufficient momentum to go 'global' are then forced to retreat to a more home region-centric strategy.*

7.4 North American core company strategies

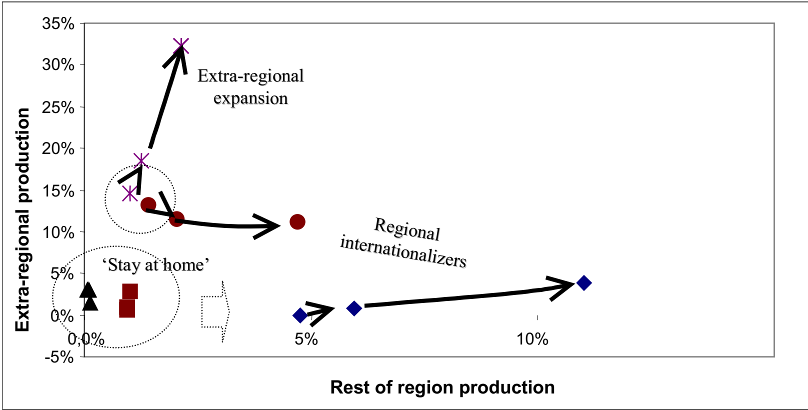
To analyze the North American subset, the strategy clusters will again be addressed on the basis of the four overarching categories. Firms will continue to be identified and clustered

by their 1990 baseline strategy classification even as their strategies change over time. At the end of the section firms will be 'reclassified' on the basis of the same general parameters used in 1990 in order to qualify the nature of the strategy migrations.

7.4.1 North American domestically-oriented companies

Domestically oriented companies form the largest supercluster of the North American firms in the sample, with 19 of the 28 also being absolutely domestic in 1990. Unlike the relative homogeneity of their European counterparts, North American domestically oriented companies pursued diverse strategies after 1990. To highlight that diversity, the firms which stood apart in their migrations from the remaining firms in their respective strategy clusters have been identified and positioned in Figure 7.16. The largest dotted circle at lower left shows the position of the supercluster in 1990, in which the exporting companies and 16 of the 19 domestic companies remained in 1991-95 and 1996-01 ('stay at home' strategy). To the right is a cluster of three domestic companies ('regional internationalizers') that made a rigorous push into Canada and Mexico (Sears, Costco and Wal-Mart), which subsequently also accounted for the vast majority of their international activity. Sears remained entirely regionally focused while Wal-Mart and to a lesser extent Costco extended their reach beyond North America, in the case of Wal-mart to Europe and even China.

Figure 7.16: Internationalization, North American domestically oriented companies (1990-2001)

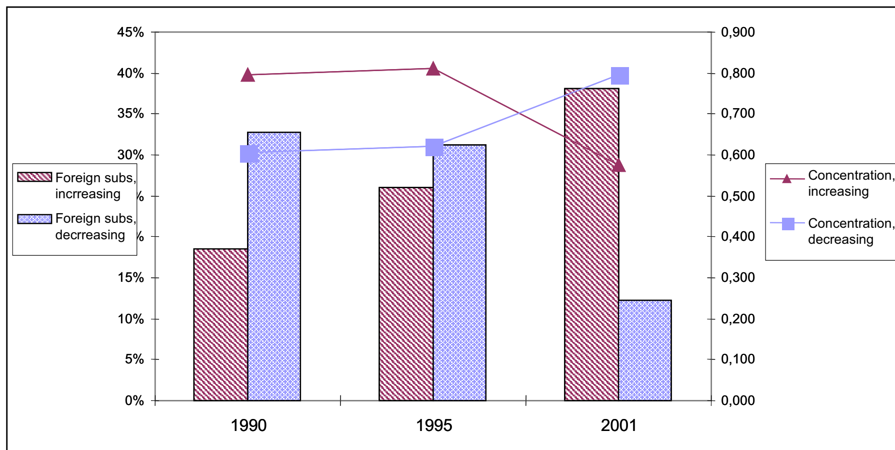


Within the DOM+ cluster (five firms; the smaller dotted circle), another split emerged between three companies which appeared to redefine their priorities (AT&T, GTE and Marathon Oil), either *de*-internationalizing (such as AT&T and GTE) or retreating to within the region, and GE and ARCO, which experienced a considerable boost in their extra-regional activity. The variety in these three strategic migrations suggests that North American companies had more options than their European counterparts, for whom a retreat to the home market was apparently unviable. This underscores earlier arguments that integration in North America is unique due to the hegemonial position of the United

States and the benefits this provides in terms of the preservation of core company positioning, even in a domestic environment.

Divergence is also apparent in the network spread data in Figure 7.17 (available for only 12 of the 28 domestically oriented companies). The available sample of 12 domestically oriented firms was split into two groups of six firms, one of which exhibited clear increase in the scale of internationalization of their subsidiary base (DOISUB) and a reduced geographic concentration of their networks (HERF). The other half, meanwhile, showed a clear decline in their subsidiary internationalization and a corresponding rise in the Herfindahl concentration value. Prominent in the latter group are the three telecom companies, AT&T, GTE (Verizon) and Bellsouth. Their changing strategies are likely related to the liberalization of the US telecommunications market after 1996, which created new growth opportunities and clearly led to a shift in priorities. The former include exporters AMR and Boeing, which the data suggest were moving away from a pure export orientation and towards increased decentralization of productive activities, as well as ConAgra, Georgia-Pacific, JC Penney and GE. A striking feature of the cluster in general is the relatively high DOISUB value given the relatively limited internationalization of production (average DOIP values of around five percent in 1990). This indicates that foreign subsidiaries for these companies are a fraction of the size of domestic subsidiaries, leading to a fairly fragmented network structure. The ability to maintain such a structure is in line with the tendency of micro-Fordist companies to maintain extensive control of their production networks, even in such a highly fragmented fashion.

Figure 7.17: Network spread, North American domestically oriented companies (1990-2001)



The organizational structure of domestically oriented companies developed quite differently for the group of internationalizing and the group of de-internationalizing firms identified above. These changes are captured in Table 7.23 below, which contains only the data for 1995 and 2001 since both the internationalization data and the network spread data clearly show that the dynamics in this cluster occurred primarily after 1995. The six firms pursuing clear internationalization strategies increased their subsidiary base from an

average of 96 in 1995 to 236 in 2001, while de-internationalizing firm networks shrank from 173 to 120 subsidiaries. Growth and contraction were also expressed primarily in the form of changes to hierarchical depth, with increases in depth leading to decreases in breadth and vice versa. Ultimately the increased foreign presence of internationalizing firms generates higher levels of cross-border linkages as well, while a retreat to the home base has the opposite effect.

Table 7.23: Organizational structure, North American domestically oriented companies (1995-2001)

	Subsidiaries		Hierarchical depth		Hierarchical breadth		Cross-border linkages	
	1995	2001	1995	2001	1995	2001	1995	2001
INTERN	96	236	4.0	5.2	47.8%	35.3%	14.0%	18.9%
DEINTERN	173	120	5.0	3.2	40.9%	54.1%	20.7%	12.9%

7.4.2 North American regionally-oriented companies

The regionally oriented supercluster is the second largest, with a total N of 18, of which 12 were classified as RDL+ in 1990. At the baseline the two true regional clusters (RDL and RMDM, representing only three firms) had a rest-of-region value of approximately 11 percent and an extra-regional value close to zero. The 15 RDL+ and RMDM+ firms had rest-of-region and extra-regional values of five and 23 percent on average, respectively. An initial analysis over time shows considerable diversity among the key strategy variables, but structuring the overall patterns in terms of increasing or decreasing over the decade as a whole reveals very real strategies (Figure 7.18).

Figure 7.18: Internationalization, North American regionally oriented companies (1990-2001)

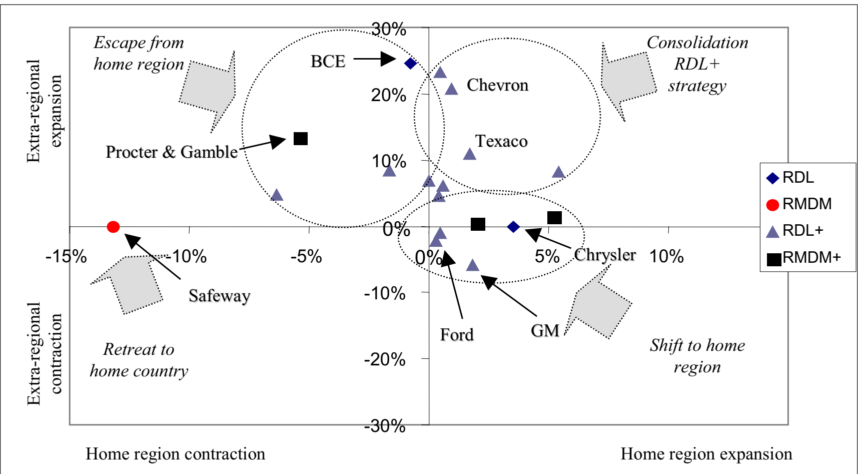


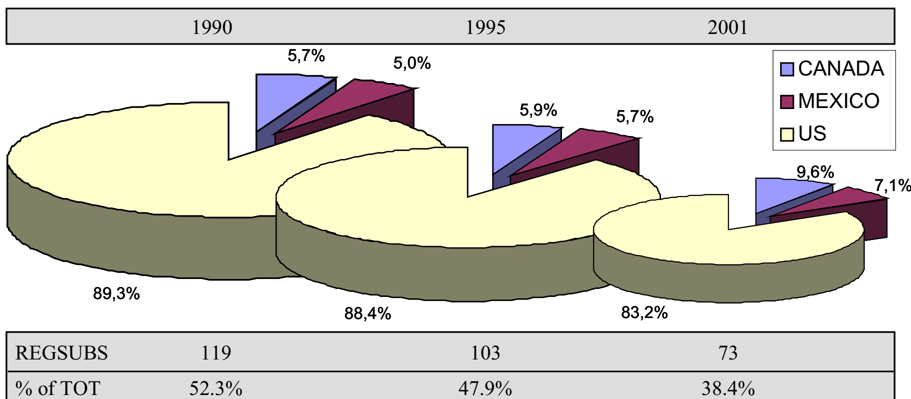
Figure 7.18 represents four quadrants, with the lower left quadrant representing a decrease in both rest-of-region and extra-regional activity (*de*-internationalization) and the upper

right an increase in both rest-of-region and extra-regional activity. The only example of the former is Safeway, which reduced its rest-of-region activity from over 22 percent in 1990 to less than ten percent in 2001 with no extra-regional strategy. The upper right quadrant is populated with a number of RDL+ firms, which in effect means an extension of their pre-existing strategy (e.g. Caterpillar, Kodak, International Paper). Firms in the upper left quadrant pursued a net shift away from NAFTA to a stronger extra-regional position. One example is Procter & Gamble, but also Canadian BCE, which was a solid regional player in 1990 but had developed an extra-regional position of over 26 percent by 2001.

The lower right quadrant entails a withdrawal from an extra-regional position and redirection into the home region. Note also that since the RORP and XRP variables combined equal the overall degree of internationalization (DOIP), if the sum of the deltas shown in Figure 7.18 is negative this also represents de-internationalization. For instance both Ford and GM reduced their extra-regional activity by a higher percentage than they increased their rest-of-region activity (circa -6 percent and +2 percent, respectively). Thus the retreat to the home region also involved retreat to the home country. The other major US automaker, Chrysler, also expanded within the NAFTA region over the period but was also the only of the Big Three to have negligible extra-regional activity in 1990 (i.e., RDL), whereas Ford and GM were already circa 25 percent extra-regional (RDL+). The merger with Daimler in effect enabled Chrysler to establish a major extra-regional presence while reinforcing its home-region foothold.

Since Figure 7.18 shows that the majority of regionally oriented companies pursued a strategy of intra-regional expansion, the question arises as to how this relates to changes in network spread. Figure 7.19 shows the average split of subsidiaries among the three NAFTA countries of all RDL+ and RMDM+ core companies for which data were available for all three years (N=13), excluding key (merged) regional players Chrysler, Amoco, Texaco and Chevron, RMDM Safeway and the one Canadian (RDL) company, BCE. A pie chart was used because concentration indices like the Herfindahl are most useful when the locations measured are more or less in balance. Changes to a Herfindahl index in the case of NAFTA, with not only a very unbalanced subsidiary spread but also a very small number of countries, would be very slight and less meaningful than the graphic representation in Figure 7.19.

Figure 7.19: Regional network spread, North American regionally oriented companies (1990-2001)



	1990	1995	2001
REGSUBS	119	103	73
% of TOT	52.3%	47.9%	38.4%

The three pie charts decrease in size over time to reflect the shrinking overall regional subsidiary base (REGSUBS). Thus the number of subsidiaries in Canada and Mexico may in fact be shrinking over time (e.g. for Mexico from 5.9 subsidiaries on average in 1990 to 5.2 in 2001), but since the domestic subsidiary base contracted more rapidly, the rest-of-region *share* of regional subsidiaries increased. Juxtaposed against this trend is the overall regional share (including domestic) relative to the total subsidiary base. The figure shows ('% of TOT') that the absolute contraction of the regional base must be seen in conjunction with extra-regional expansion of the subsidiary base. This corresponds generally to the extra-regional expansive character of 'regional-plus' firms.

Since Figure 7.18 showed that most regionally oriented firms have expanded their rest-of-region activity, the shrinking subsidiary base must be seen in this context. For the 13 firms in Figure 7.19, the average rest-of-region production share climbed from 4.3 percent in 1990 to 4.8 percent over 1991-1995, and finally to 5.1 percent over 1996-2001. In the meantime their average domestic share was reduced from 71.5 percent in 1990 to 67.4 percent in the first period and 65.4 in the second period. These shifts in the geographic scope of strategy correspond precisely with changes in network spread. Total regional activity and the regional subsidiary base declined in relation to total activity and total network spread, and within the region there was a relative shift towards Mexico and Canada. In conjunction, the burden of an increase in intra-regional activity was borne by an ever-shrinking number of subsidiaries, indicating a tendency to rationalize activities on a regional scale.

Rationalization is evidenced in fact by changes to the organizational structure of regionally oriented firms. Table 7.24 shows how the overall subsidiary base contracted over the decade (while Figure 7.19 shows that the regional subsidiary base contracted even more quickly), but that contraction was not at the expense of hierarchical depth or breadth. In fact, the network breadth variable (PRIM) remains constant for the group while hierarchies continue to deepen over the decade (MXLEV). This suggests that 'dead-end' branches of the corporate tree were being pruned while the hierarchy around core activities was being deepened. The modest decline in the share of cross-border linkages between subsidiaries indicates that the 'dead-end' branches were mainly domestic subsidiaries with a very small number (e.g. one or two) subsidiaries of their own located in foreign countries. This combination of dynamics can be described as a streamlining of organizational structure.

Table 7.24: Organizational structure, North American regionally oriented strategies (1990-2001)

	1990	*1995*	*2001*
TOTSUB	226.5	210.6	186.2
PRIM	35.1%	34.6%	36.4%
MXLEV	4.9	5.2	5.9
CBL	40.0%	43.4%	35.5%

7.4.3 Bi-regionally oriented companies

The extra-regional character of their spatial organization is the basic characteristic of bi-regionally oriented companies. Yet the North American bi-regional supercluster (N=11) shows a striking similarity to its European counterpart in that it too experienced a relative *decline* in extra-regional activity, particularly after 1995. Only three companies (Hewlett-Packard, Motorola and Dow) expanded extra-regionally after 1995, raising their XRP share from 41 percent in 1991-95 to 45 percent in 1996-01. The remaining eight in fact retreated from their extra-regional position, as shown in Table 7.25.

Table 7.25: Intra- vs. extra-regionality, North American bi-regionally oriented companies (1990-2001)

		Rest-of-region (RORP)			*Extra-regionality (XRP)*		
	N	1990	1991-95	1996-01	1990	1991-95	1996-01
XRP incr	3	2.1%	2.4%	2.8%	40.9%	41.0%	45.0%
XRP decr	8	4.7%	5.4%	5.8%	39.1%	41.6%	36.3%

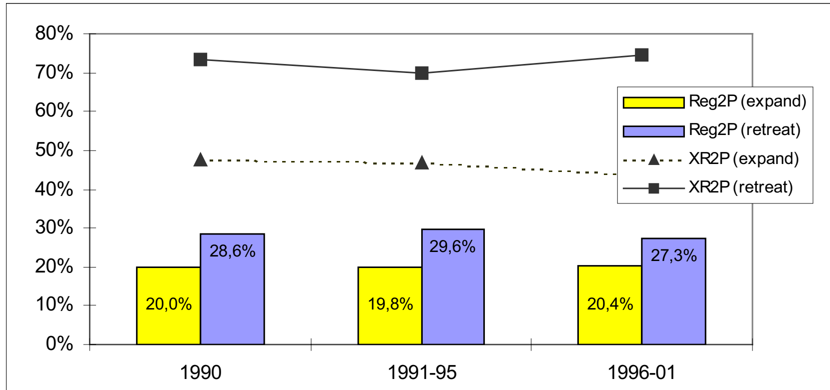
The table shows the average RORP and XRP values for firms whose extra-regional activity increased and those for whom it decreased. Both groups exhibit nearly identical extra-regional shares of activity in 1990 and from 1991 to 1995. Subsequently, however, their trajectories diverged to such an extent that their respective XRP values in the period 1996-2001 were nearly 10 percentage points apart (36 percent and 45 percent). The data also show that both groups continued to expand into the home region over the decade as a whole. However, the increase in RORP after 1995 for the latter group (from 5.4 percent in the first period to 5.8 percent in the second) does not account for the dramatic drop in extra-regionality. This means that the extra-regional contraction was a matter of overall *de-internationalization*. While the overall degree of internationalization for both groups was quite comparable in 1990 (approximately 43 percent), after 1995 firms in retreat had an overall DOI of 42 percent compared to the 49 percent of firms in extra-regional expansion. Alternately, this means firms in retreat had increased their overall home region position (including domestic) from 61 percent in 1990 to 64 percent after 1995, while the regional position of firms in expansion declined from 59 percent to 55 percent.

Firms which expanded extra-regionally after 1995, however, had a markedly lower rest-of-region share of activity than firms which reduced their extra-regional position. This suggests once again that firms pursuing bi-regional strategies in 1990 were forced to choose focus after 1995, either to opt for an expansionist global strategy or consolidate within the home region. *Only the few bi-regional firms with a relatively modest home-region position in 1990 were able to pursue continued global expansion, while for those with a more solid regional base opted for consolidation within the home region.*

As in the case of extra-regional retreat by European firms, the withdrawal by North American companies is best qualified by considering shifts in the share of activity in Europe (RG2P), and Europe as a percentage of overall extra-regional activity (XR2). Figure 7.21 shows the average values for RG2P and XR2 for the three firms which continued to expand extra-regionally compared with the values for the eight firms in retreat. Firms in extra-regional retreat withdrew slightly from Europe, which declined as a share of the total from over 29 percent in the first period to just over 27 percent in the

second. However, retreat from other extra-regional locations was more significant, evidenced by the post-1995 *increase* in Europe as a share of overall extra-regionality.

Figure 7.20: Extra-regionality, North American bi-regionally oriented companies (1990-2001)



A significant difference between the two groups is also formed by the share of overall extra-regionality accounted for by Europe. Firms pursuing an expansionist strategy, already with limited home-region positions (see above), also had relatively limited European positions. Their European activity hovered at the 20-percent mark and this amounted to less than half of their extra-regional activity (XR2). This means that *the bi-regional firms on a globalizing trajectory were less home- and host-regionally organized to begin with than firms which retreated to the home region and, within their extra-regional retreat, consolidated in Europe*.

Note also that two of the three in expansion were 'bi-regional plus' and seven of the eight in retreat were 'bi-regional'. Clearly the latter are more sensitive than the former to regionalism as a 'gravitational' force in *both* regions. That difference embodies the distinction between the two bi-regional types and as such the strategic clustering in 1990 was in itself a valid 'predictor' of strategic migrations to come. These developments are only partially evident in the network spread data. The clustering of expansionist / retreating firms employed above showed little to no difference and thus the network spread data, available for the nine of the eleven bi-regional firms (excluding Compaq and Digital Equipment) were aggregated in a single table (Table 7.26).

Table 7.26: Network spread, North American bi-regionally oriented companies (1990-2001)

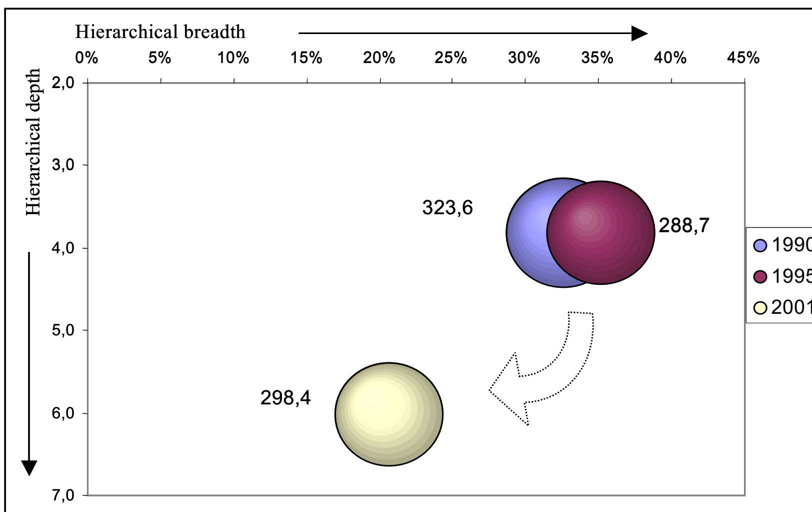
	1990	1995	2001
DOISUB	75.7%	70.2%	77.9%
HOSTC	38	43	39
HERF	0.317	0.327	0.364
RORSUB	5.5%	5.2%	3.9%
EURSUB	43.0%	37.8%	46.7%

The data paint a mixed picture of modest fluctuations in internationalization of the subsidiary base and the number of host countries. The only indication of the pattern of regional retreat discerned above is given by the overall concentration index (HERF), which rose moderately over the decade. To explore whether this rise was related to a consolidation of the North American and European position, and thereby 'bi-regionality' in general, the percentage of the subsidiary base in Europe was also calculated (EURSUB) and that of the rest of North America (RORSUB).

The data do substantiate the general consolidation across two regions. Since the drop in the European share of the subsidiary base from 1990 to 1995 (43 to 37.8 percent) was compensated by an increase in the domestic share of subsidiaries (i.e., a drop in DOISUB from over 75 percent to less than 71 percent), the data suggest that shifts in the subsidiary network occurred overwhelmingly between the home country and Europe. In the meantime the role of Mexico and Canada in the bi-regional strategy showed a gradual decline (and within that decline a slight shift away from Canada and towards Mexico). Combined, the domestic share of subsidiaries together with the rest-of-region and Europe were strikingly stable, accounting for 72.8 percent of all subsidiaries in 1990 and 72.7 percent in 2001.

Organizationally, bi-regional firms followed a similar path as regionally oriented firms as well as their European counterparts, involving a reduction in network breadth and an increase in network depth. Figure 7.21 shows these two dimensions along the horizontal and vertical axes, respectively. In terms of depth there was essentially no change between 1990 and 1995, while there was a slight increase across the horizontal. After 1995, however, bi-regional firms became significantly more vertical in orientation, with a jump in depth from fewer than four levels in 1995 to six in 2001 and a reduction in breadth from over 30 percent in 1995 to 20 percent in 2001. In terms of overall network size, bi-regional firms changed little, hovering just above or just below 300 subsidiaries.

Figure 7.21: Organizational structure, North American bi-regionally oriented companies (1990-2001)



7.4.4 North American globally oriented companies

The globally oriented supercluster comprises only three firms (Exxon, Mobil and Coca-Cola) and is thus too small to speak of 'general trends'. Moreover, the former two, both globally integrated petroleum companies, merged in 1999 such that only one GLOB and one GLMDM firm remained at the end of the decade. For globally oriented companies, the analysis centers on their extra-regionality. Figure 7.22 shows (schematically) the extra-regionalization paths of all three globally oriented companies from 1990 to 2001, with the dotted vertical line representing the year before the ExxonMobil acquisition and thus the last year in which both companies reported independent data.

Figure 7.22: Internationalization, North American globally oriented company strategies (1990-2001)

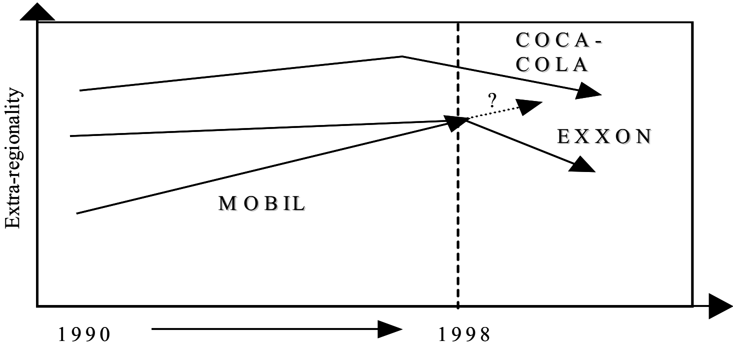


Figure 7.22 shows that all three companies were increasingly extra-regional from 1990 on. Mobil made the steepest ascent, climbing from just under a 50-percent extra-regional position in 1990 to over 54 percent over 1991-95. Coca-cola's climb had the next largest slope and Exxon had the flattest trajectory of the three. In 1990, Exxon had an XRP share of over 58 percent compared to Mobil's 49.5 percent, but by 1997, both had XRP shares of around 60 percent. Just at the point where Mobil's apparent trajectory was about to carry it past Exxon in terms of its extra-regional position (indicated by the dotted arrow and question mark in Figure 7.22), it was acquired by Exxon. Since the two had compatible geographic 'portfolios' of activity, the subsequent decline in Exxon's extra-regional (and thus international) position was not attributable to a 'one-off effect' of the acquisition. Exxon's contraction was part of a strategy to reduce the 'overlap' between the two companies' production networks and to alleviate risk exposure in the wake of the acquisition by retreating to the home base. Strikingly, Coca-Cola's extra-regional position began to contract around the same time, such that both surviving globally-oriented American firms ended the decade on a downward slope. This suggests that globalization strategies from the North American context, already rare before 1995, had become less viable in the years that followed.

Since this was not the case for European globally oriented companies, and those companies operated in the same sectors (PETR and FOOD), it is possible that the difference is rooted in the gravitational pull of the US, i.e. a 'large home country' effect. Similar patterns were described for bi-regional companies above. That withdrawal was

largely at the expense of Europe, since the RG2 data for all three companies (Table 7.27) shows a slight increase in Europe's share of these companies' activities from 1990 to 1991-95 before dropping more sharply in 1996-01. However, the fact that the XR2 variable dropped over both periods indicates that the increase in RG2P over 1991-95 was offset by a larger expansion outside of Europe (and the home region). Thus the pre-1995 period was one of overall extra-regional expansion, in which Europe played an important (but not leading) role, and the post-1995 period was one of overall extra-regional retreat.

Table 7.27: The European presence of North American globally oriented companies (1990-2001)

	1990	1991-95	1996-01
Europe as share of total	23.2%	24.6%	15.4%
Europe as share of extra-regional	44.0%	41.7%	25.5%

Changes in production networks due to reduced 'overlap' can be seen partly through an analysis of the network spread data, which by 2001 reflects the integration of Exxon and Mobil. The data for Exxon (ExxonMobil) are shown in Table 7.28, with Coca-Cola included for comparison. The table shows that Exxon(Mobil) sharply reduced its foreign subsidiary base over the decade, but most pronounced after 1995, when its DOISUB share dropped from 78 to 60 percent. Thus the scale of activities in foreign countries was being reduced, but not the geographic scope of its global strategy. At the same time, the number of host countries in its network had increased by 50 percent from 1995 to 2001, climbing from 30 to 45.
This suggests that the spans of their respective subsidiary networks were complementary across their geographic base. Of the 30 countries Exxon was active in and the 35 countries Mobil was active in, there was an overlap of 19 common countries, of which 15 were developed countries with few or no oil reserves of their own. Thus Exxon and Mobil were largely active in different countries and brought together a geographic network of significant international scope. Coca-cola, for its part, followed a more or less identical path, reducing its foreign subsidiary base but increasing the number of host countries and maintaining a fairly stable degree of concentration (HERF). The internationalization and network spread data together indicate some level of 'overstretch' in the early- and mid-1990s which resulted in untenable positions.

Table 7.28: Network spread, Exxon / ExxonMobil and Coca-Cola (1990-2001)

	Foreign subsidiaries			Host countries			Concentration index		
	1990	1995	2001	1990	1995	2001	1990	1995	2001
Exxon(Mobil)	85.5%	78.0%	60.2%	27	30	45	0.348	0.376	0.339
Coca-Cola	73.0%	77.3%	70.9%	20	27	31	0.284	0.273	0.287
AVG	79.2%	77.7%	65.6%	24	29	38	0.316	0.324	0.313

The apparent consolidation of activities after 1995 should be evident in the firms' organizational structures.Table 7.29 shows that Exxon's subsidiary base expanded over the

decade as a whole, but that the expansion prior to 1995 was one of breadth as opposed to depth, whereas its network after 1995 deepened both relatively and absolutely, no doubt due to the absorption of Mobil's activities. The enhanced streamlining of its organizational structure is also demonstrated by an increase in cross-border linkages after 1995 (from 24.5 to 29 percent) despite the overall reduction in the foreign share of the subsidiary base. That means that host country networks were considerably 'leaner' and spanned more countries in the second half of the decade than in the first.

Table 7.29: Organizational structure, Exxon / ExxonMobil and Coca-Cola (1990-2001)

	Subsidiary base			Hierarchical breadth			Hierarchical depth			Cross-border linkages		
	1990	1995	2001	1990	1995	2001	1990	1995	2001	1990	1995	2001
Exxon(Mobil)	166	200	244	25.5%	31.5%	24.5%	6	5	8	29.5%	24.5%	29.0%
Coca-Cola	122	75	79	8.2%	14.7%	31.6%	8	6	5	28.7%	52.0%	54.4%
AVG	144.0	137.5	161.5	16.9%	23.1%	28.1%	7.0	5.5	6.5	29.1%	38.3%	41.7%

Joining forces was part of an internationalization strategy for both companies. Analyzed as a (fictitious) combined entity over the entire decade (in effect weighing for size and differences in geographic scale and scope), their internationalization data exhibit surprising stability. For the combined entity the overall degree of internationalization climbed from 63 percent in 1990 to 64.5 percent over 1991-95, holding steady over 1996-01 at 65.3 percent. The extra-regional share followed the same path, rising from 55.6 percent in 1990 to 57.3 over the first period and again remaining constant thereafter at 57.2 percent. The combined entity's rest-of-region share actually *climbed* after 1995, from 7.2 percent over 1991-95 to 8.1 percent over 1996-01.
Coca-Cola, meanwhile, had significantly reduced its European activity, from 40 percent in 1991-95 to just 20 percent in 1996-01 (seen also in the rising HERF index). There was still a noticeable increase in the number of countries with productive activity over both periods and a general reduction in the size of the subsidiary base, suggesting that Coca-Cola was trimming the fat at all levels. The modest size of its subsidiary base stands in stark contrast with the European GLMDM companies, which are many times larger. Coca-Cola's tendency to work through licensed bottling operations makes its control strategy more one of 'core technologies' (the secret Coca-Cola recipe) than one of direct management control. This is quite possibly the only way in which a non-vertically integrated company from a micro-Fordist environment can attain global status, through the use of 'soft control' tactics that permit centralization within a decentralized industry (cf. also for example McDonald's).

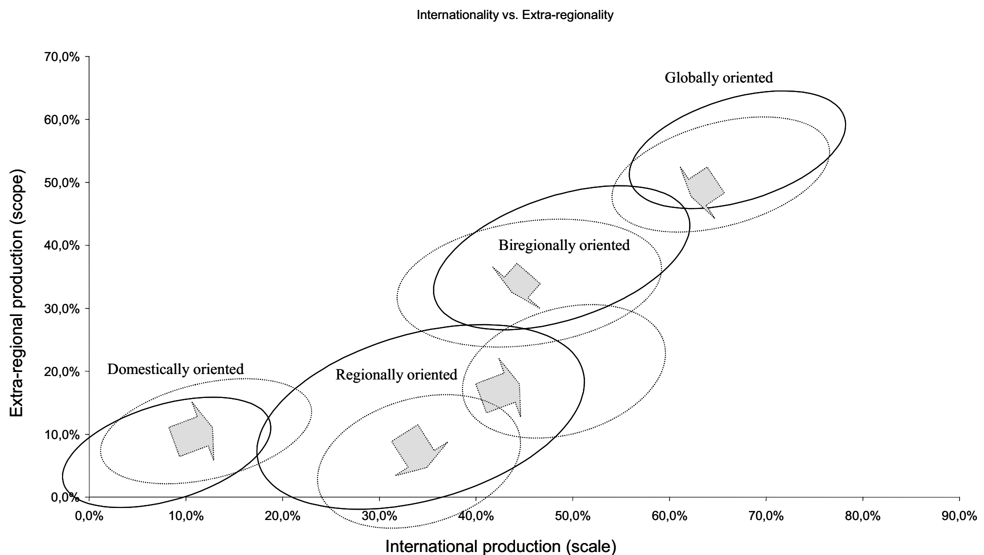
7.4.5 Interim conclusions, pt. 2

The strategy migrations pursued by North American core companies are in most ways similar to the strategies of their European counterparts. The overall trend towards more international activity, both inside and outside (although to a lesser extent in relative terms) the NAFTA region, is undeniable, yet there are some differences. As a whole, internationalization strategies for North American core companies can be said to have converged, with the least international in 1990 becoming more so over the decade and the

most international in 1990 becoming less so. This shrinking bandwidth is evident in Figure 7.23, which shows the migrations for the 52 surviving North American core companies in 2001.

While domestic companies have internationalized to some extent, many have remained (absolutely) domestic, showing that the US as a home base can still guarantee a relatively secure position for its core companies, even within the context of the NAFTA. Regionally oriented firms show divergent tendencies, with some firms retreating into the home region and even home country, and others moving out of the regional orbit. Ironically, therefore, a strictly regional strategy appears an insufficient basis for maintaining a core strategy, especially when one considers the overrepresentation of regional firms in the wave of acquisitions.

Figure 7.23: Strategy migrations, North American core companies (1990-2001)



For the bi-regional supercluster as a whole, strategies became less extra-regional and more concentrated, in some cases in the home region and in others focused on the two core regions. This suggests that from the North American context regionalism may have polarized the strategy field, inducing some firms to concentrate on protecting the regional base of their core position and others to 'escape' the confines of the home region and reconstitute that position on the basis of geographic spread. Globally oriented companies, even taking the acquisition of Mobil by Exxon into account, were apparently subject to similar pressures as bi-regional firms and ended up *in retreat* after 1995, both towards the home country and the home region.

If the 52 surviving firms were reclassified in the strategy typology according to their activity in 1996-01 (Table 7.30), the changes would be less dramatic than for European core companies. Only twelve companies changed their classification. The changes in Table 7.30 are in part a reflection of new cluster membership, i.e. through new companies joining

the cluster and others migrating to other clusters. The changes are also due to fluctuations in the internationalization variables of companies that stayed in the cluster. There were, for instance, fewer domestic firms (from 19 down to 16), but the remainder had slightly higher internationalization values. There were only three of the four exporters left, with one having been promoted to the ranks of the DOM+. The true regional category had disappeared altogether, and several of the RDL+ firms were able to make the jump to a bi-regional classification. In turn, some of the bi-regional companies fell back to RDL+ status such that the cluster did not grow substantially with respect to 1990. The globally-oriented supercluster remains changed only in name (and the underlying values), with one entity now representing the two GLOB firms of yore and Coca-Cola remaining the only GLMDM.

Table 7.30: Reclassification of North American strategy types based on average values 1996-2001

STRAT	N (1990)	N (2001)	XRP_90	XRP_1996-01	DOIP_90	DOIP_1996-01
DOM	19	16	2.1%	2.4%	0.5%	0.6%
EXP	4	3	1.6%	0.0%	1.4%	0.0%
DOM+	5	4	14.4%	13.5%	12.7%	11.5%
RDL	2	0	12.3%	,	1.0%	,
RMDM	1	0	22.0%	,	0.0%	,
RDL+	12	10	28.4%	28.9%	23.1%	24.7%
RMDM+	3	5	31.8%	29.7%	26.4%	21.2%
BiRDL	6	5	44.8%	44.7%	38.6%	37.9%
BiRMDM	2	2	46.3%	44.6%	41.5%	41.3%
BiRDL+	3	5	41.4%	46.2%	40.3%	41.2%
BiRMDM+	0	0	,	,	,	,
GLOB	2	1	61.2%	64.7%	53.9%	56.1%
GLMDM	1	1	60.6%	66.1%	54.0%	59.6%
Total	**60**	**52**	**20.7%**	**23.2%**	**17.2%**	**19.7%**

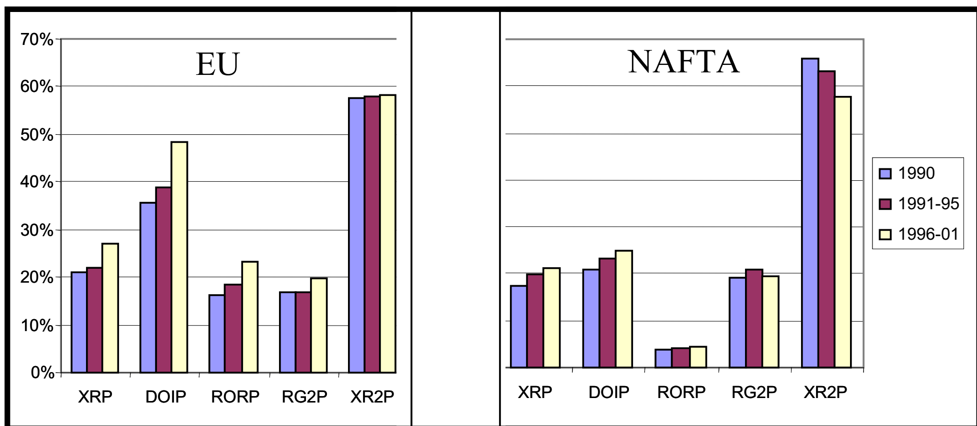
7.5 Contrasting European and North American patterns

The European and North American subsets can be compared and contrasted along the most important dimensions of analysis: scale and scope of internationalization (Figure 7.24). Both subsets exhibit similar trends in that both are increasingly international, increasingly extra-regional and increasingly regional. European core companies are more international, and have been internationalizing much more quickly, than their North American counterparts. In both cases the absolute gains in internationalization were primarily extra-regional.

Yet considering that the rest of Europe as a ‘host’ for European core companies is much smaller than the extra-regional world, the home region was ‘pound for pound’ the main beneficiary of the internationalization push among European core companies, particularly after 1995. Also taking into account the relatively small size of the North American ‘host’ region (de facto Canada and Mexico), intra-regional growth for North American core companies has been considerable. The size of the home country is shown to be a

determinant of overall internationalization levels, with companies from large countries such as the US being on average less international than firms from medium-sized or small (European) countries. North American and European core companies are however *equally regional*, suggesting that North American and European companies have established a balance of power from a regional perspective.
European companies aimed more of their extra-regional activity at North America than vice versa. For both sets of companies, but particularly for the North Americans, increased extra-regional activity is aimed less and less at the second region. Europe represents a relatively steady share of overall North American core company activity (RG2P) while it is in fact declining in its relative importance as an extra-regional base (XR2P).

Figure 7.24: Mean values for key strategy variables, EU vs. NAFTA core companies (1990-2001)



Taken as a whole these trends point to some degree of convergence with respect to the activities of both groups in each other's region (note that this is a subset, N=72, consisting of all firms with at least ten percent of their activity in the second region in 1990). In 1990, European core companies had just under 16 percent of their activities located in North America (RG2P) to North American core companies' 19 percent in Europe. In the course of the second period both had converged to just under 20 percent. The same is true of the extent to which the second region (XR2P) accounts for total extra-regional activity (XRP). In 1990, the average European core company had just under 58 percent of its activity located in North America and the average North American company nearly 66 percent located in Europe. By 1996-01 both had converged to around 58 percent. This apparent 'harmonization' across regions may be an indication that on the one hand 'globalization' leads to strategic convergence, and on the other hand that 'regionalism' has possibly created a stalemate between the world's two major RIAs.
At the level of individual clusters, the two subsets exhibit a number of similarities as well as discrepancies. Domestically oriented companies in both regions were the most likely to make substantial gains in their overall internationalization, particularly intra-regionally. Regionally oriented companies tended to consolidate within the home region, with only a

few 'migrating' into a bi-regionally oriented strategy. Bi-regionally oriented companies from both regions tended to become less extra-regionally oriented over the decade, and those that became more extra-regional tended to concentrate that extra-regional activity more and more in the second ('host') region. This suggests that regionalism exerts a gravitational pull on the geographic spread of activity, from which only the most highly internationalized companies can break free. For bi-regionally oriented companies that creates a 'chasm' between the regional and the truly global that few were able to leap across.

8. SYNTHESIS: OPENNESS AND THE MACRO-MICRO LINK

One of the key conclusions in Chapter 2 was that the mainstream literature on regional integration tends to be macro-oriented. Core companies and their strategies form the bridge between the macro- and micro-levels of analysis. They control, both directly and indirectly, significant volumes of economic activity. In Chapter 5, trends at the macro-level were analyzed on the basis of trade and investment data to draw conclusions about the level of inward- and outward openness of the SEM and the NAFTA. In Chapters 6 and 7, trends in the spatial organization of core companies from both were analyzed on the basis of their internationalization of production, network spread and organizational structure. Since core companies are the lynch pin between the micro and macro levels of analysis, discussing their activities at the *aggregate* level can reveal a great deal about larger economic shifts and ultimately about regional openness. It must be recognized, however, that such an analysis distorts the firm-level perspective by overemphasizing the largest firms. In the end this distortion is a major component of the 'level of analysis problem' identified in Chapter 2.

8.1 Openness in European competitive space

The most crucial form of openness from the policymaker's perspective is inside-in, or the degree to which insider companies interpenetrate each other's home markets. The second form of openness is that of outward openness (from the inside-out), or the tendency regionalism has to foster extra-regional expansion. Thirdly, inward (outside-in) openness will be discussed, meaning the scale and scope of outsider firm activity (North American firms in the case of Europe and vice versa). Although theoretically outside-out openness was addressed in Chapter 3, it falls beyond the scope of the micro-level data under consideration in this study. For such analysis 'third party' firm activity in the world beyond North America and Europe would need to be considered; this remains a focus for future research.

8.1.1 Inside-in openness, Europe

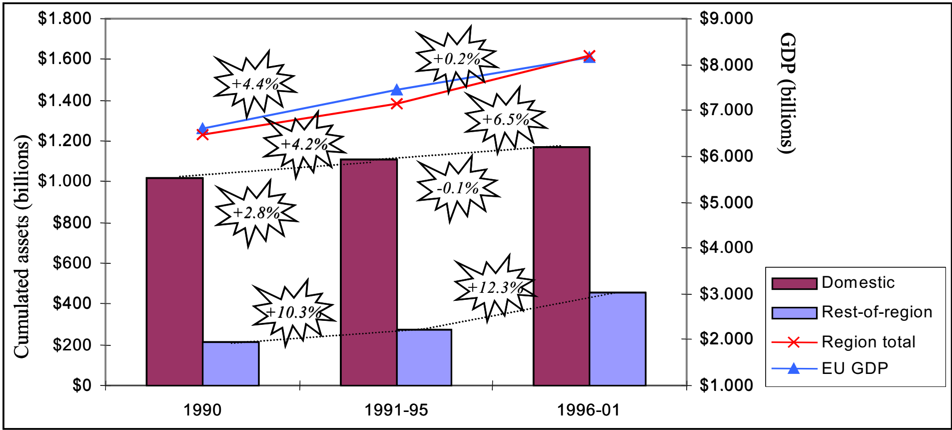
There are several ways in which inside-in openness can be investigated with the data at hand. Firstly, on the basis of the aggregated value of production of all the companies in question within Europe. This also removes the problem of whether or not to omit firms which have been acquired (as shown above almost exclusively at the hands of other core companies), since their activity will have been absorbed by the acquiring firm and thus will still be reflected in the aggregate numbers. If the acquisition was cross-regional, the economic activity remains more or less in the same location but through the change of ownership, becomes e.g. part of the 'outside-in' instead of the inside-in perspective. Analysis in this way also biases the outcomes towards the larger firms, but remains a representation of overall economic activity if ownership is not considered.
Aggregating asset positions creates a possibility of bias through exchange rate fluctuations. For instance, a European firm's assets in the US may appreciate, and therefore take on a larger significance in the firm's overall portfolio, simply through an appreciation of the dollar relative to the Euro. No attempt is made here to correct for this potential bias, on the

one hand for technical reasons of feasibility and on the other to maintain a level of 'strategic reality' in the analysis.

Technically, it would be nearly impossible to correct for exchange rate effects because there is no universal adjustor for companies with a complex geographic spread of activities. It would be nearly impossible to recalculate the value of activity in any given country because these have already been converted from host-country currencies to home-country currencies and aggregated in the annual report. Given the level of geographic disclosure provided in the average company annual report, individual countries (within the geographic segments reported) could only be indicatively aggregated and weighted, introducing other possibilities for random bias.

Strategically, the appreciation of US assets in the aforementioned example is relevant not only because it reflects a real situation that affects business behavior (such as the ability to export or the cost of borrowing capital), but also because it affects the firm's relative bargaining power and positioning in the host country. This latter consideration is very much in keeping with the strategic actor approach central to this study (see Chapter 3). Figure 8.1 shows the cumulative domestic and rest-of-region positions for European core companies as a group against the backdrop of regional GDP growth.

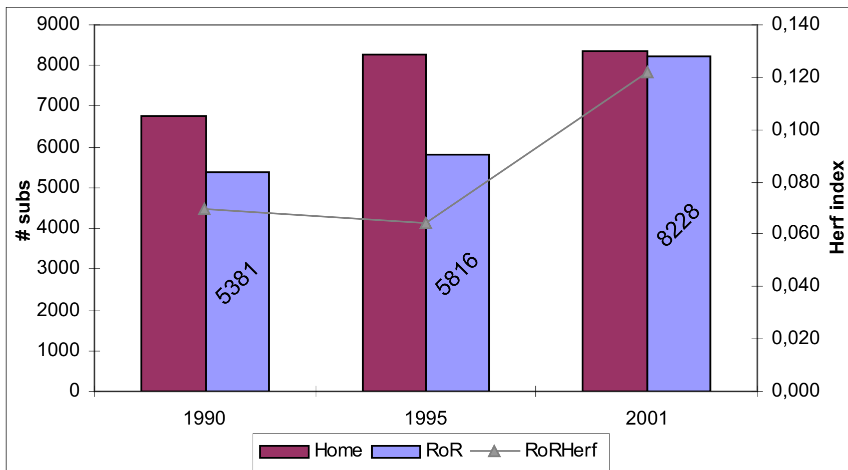
Figure 8.1: European core company regional production (agg.) vs. EU GDP (1990-2001)



The values are shown in US dollars, which introduces an additional bias through exchange rate fluctuations. However, since the companies in question themselves report in different currencies, and through their international activity carry exchange rate fluctuations over into their balance sheets, correcting for that bias becomes impossible without knowing the exact value of activities in distinct countries for each firm in each year, or being able to make corrections for e.g. transfer pricing and arbitrage activities. The figures also reflect other Europe besides the EU15, since most companies do not specify the one versus the other (see Appendix II). However, the circa 14 companies which did make such a distinction had on average less than five percent of their European activity in non-EU Europe. Therefore the figures may overstate the case slightly but as an indication continue

to serve the purpose. The figure gives a general idea of (changes to) the dollar value of core company assets and European GDP over time. Because the measurement points are in fact not equidistant, as the figure would suggest, the slopes for each variable over the first and second periods have been calculated and superimposed to correct for that bias.
Figure 8.1 shows that the value of total regional productive capacity, measured by assets, grew on aggregate at approximately the same pace as overall EU GDP over the period 1990-1995 (just over four percent). Decomposed to its domestic and rest-of-region segments, the slopes show that rest-of-region production grew considerably more rapidly in relation to its initial size while domestic productive capacity grew more *slowly* than European GDP. More importantly, both domestic capacity and European GDP slowed dramatically over the second period, while the high growth rate for rest-of-region productive capacity accelerated to a slope of over 12 percent. Intra-regional expansion, and thus inside-in openness was already considerable in relative terms before 1995, but afterwards it continued to accelerate even as growth in GDP and domestic core company activity came to a halt. Collectively, the rest-of-region position of European core companies *increased sharply* over the decade, from *17 percent* of the total regional position (DOM plus ROR) in 1990 to *28 percent* over 1996-01. Moreover, the rise in RoR productive capacity relative to EU GDP took place at the hands of a smaller number of firms due to the mergers and acquisitions over the period. Even though assets and GDP cannot be directly related, the pattern suggests that Europe became increasingly open from an inside-in perspective, and that the increase in openness led to a concentration of economic power amongst core companies relative to the rest of the economy.
An 'unweighted' analysis of interpenetration can be performed using the subsidiary data to analyze the intra-regional structure of core company network organization. A first step is to compare changes to the total number of foreign subsidiaries *within the EU15* to the number of domestic subsidiaries controlled by European core companies (Figure 8.2).

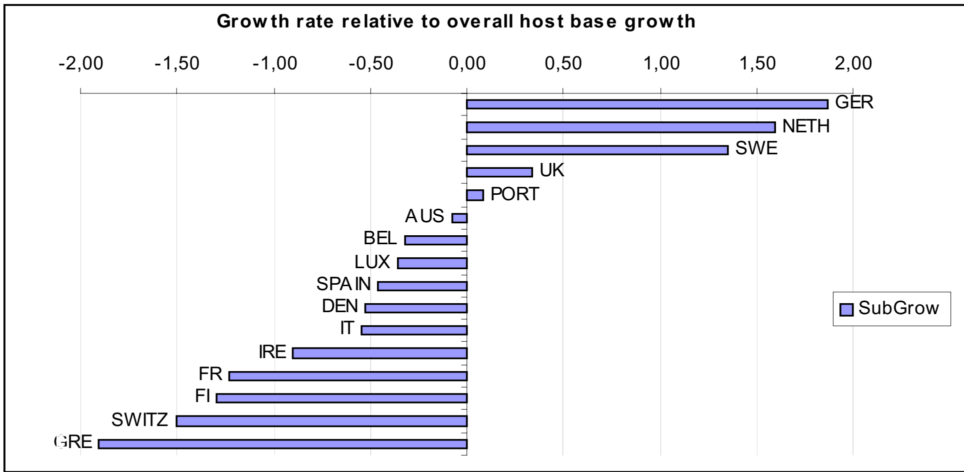
Figure 8.2: Inside-in network spread, Europe (1990-2001)



The figure shows the cumulative population of domestic subsidiaries versus host-country subsidiaries within the EU15 (plus Switzerland), where in the first period the rest-of-region (host) subsidiary base increased only slightly and the domestic subsidiary base increased by a considerable margin. By 2001, however, the balance had shifted such that the two were nearly equal. To illustrate, the total host subsidiary base for the European set rose from 19,936 in 1995 to 21,360 in 2001, an increase of 8.6 percent. The rest-of-region (RoR) host subsidiary base, meanwhile, rose from 5816 to 8228 over the same period, an *increase of over 40 percent*. At the same time the RoRHerf index, which reflects the relative concentration of *host* subsidiaries among the member countries (i.e., not including domestic subsidiaries), nearly doubled after 1995, indicating that the growing subsidiary base in the EU was increasingly unevenly distributed.

That uneven distribution can be qualified by considering the growth rates for the host subsidiary base in individual European countries relative to the whole (Figure 8.3). Since analysis in Chapter 7 established that the bulk of change took place in 1996-01, Figure 8.3 represents changes from 1995 to 2001 only. Given that the growth rate for the RoR subsidiary base from 1995 to 2001 was 40 percent, Figure 8.3 shows that the host base grew for only four countries more rapidly than the overall regional growth rate. Germany topped the list with a growth rate nearly double the overall growth rate, followed by the Netherlands and Sweden.

Figure 8.3: Inside-in shifts in host subsidiary base (relative to average), Europe (1995-2001)



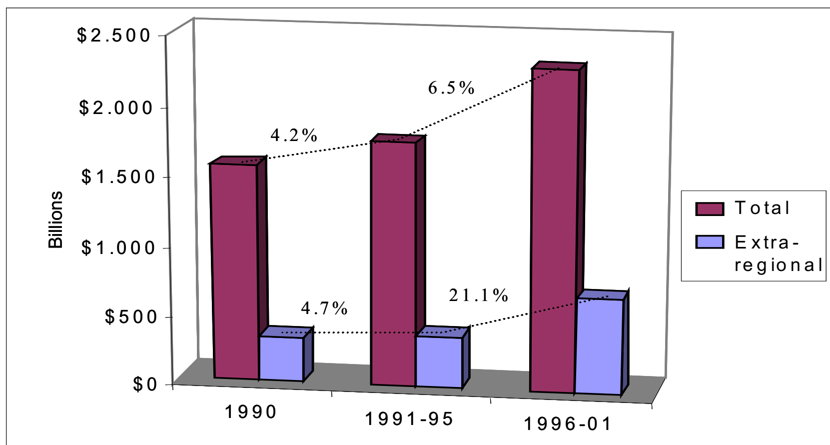
The UK, whose subsidiary base accounted for approximately one quarter of the regional total, grew about thirty percent faster than the region as a whole. Since these were among the largest host countries to begin with, their higher growth rates carried the region. The countries with values between 0 and –1 are those which grew in absolute terms, but relatively more slowly than the whole, and countries with values below –1 (Greece, Switzerland, Finland and France) experienced a *decline* in their overall host subsidiary base. Thus it seems that *inside-in openness was particularly favorable to the traditional*

'core' countries of the region, drawing a parallel to the world of core companies. France, and to a lesser extent Italy, forms a notable exception.

8.1.2 Inside-out openness, Europe

The second form of openness to consider is from the inside-out; that is, the tendency for regional insiders to engage in extra-regional activity. As in the case of 'rest-of'-region' growth, the aggregate value of extra-regional activity can be examined to draw conclusions on the overall 'outward position' of the core company base in question. Figure 8.4 shows the aggregate extra-regional position, in billions of US dollars, compared to the total for the European core company set. In absolute terms, the total value of assets under European core company control grew from $1.5 trillion in 1990 to $1.7 trillion in 1995, while the extra-regional aggregate grew from $327 billion to $373 billion. Their respective growth rates are nearly identical at just over four percent per year, respectively. From 1995 to 2001, the total grew to $2.3 trillion and the extra-regional aggregate grew to $684 billion. These increases represent average growth for the total of 6.5 percent, but over 21 percent for the extra-regional share. As a result, the aggregate extra-regional component increased as a share of the total from 22 percent over 1991-1995 ($373 divided by $1,700) to nearly 30 percent ($684 divided by $2,300) over the period 1996-01. *After 1995, the extra-regional share of European-owned economic activity increased dramatically*.

Figure 8.4: Total vs. extra-regional productive capacity (agg), European companies (1990-2001)



Of the aggregate extra-regional position, less than half was located outside North America in 1990 ($129 billion, or 39 percent). In the period after 1995, however, that number had climbed to $362 billion, or 53 percent of the total value of extra-regional activity. Thus there was a clear tendency towards general inside-out expansion, more than an outside-in response to the NAFTA (see below). Extra-regional growth is likely to be reflected in changes to the number of countries in which European core companies operated, particularly in the second half of the 1990s. Data was found on European core company subsidiaries in a total of 124 countries in 1990, excluding the EU15+Switzerland. By 1995,

16 new countries were included in the aggregate subsidiary network, four of which did not formally exist in 1990 (Croatia, Czech Republic, Slovenia and Slovakia). At the same time, five countries no longer appeared in the network (Burundi, Tahiti, Gibraltar, Iceland and the Northern Mariana Islands), bringing the total (ex EU) to 135. In 2001, another 18 countries were excluded, 12 of which were located in Africa, with the remainder in Asia and the Caribbean. A number of new countries had been included as well which also had not existed in 1990, such as Estonia, Latvia, Uzbekistan, Kazakhstan and Lithuania, bringing the total to 124. Table 8.1 groups host countries by geographic region. The HERF index used here is the spread of *host subsidiaries only*, that is excluding the position of domestic subsidiaries in their home countries.

Table 8.1: Geographic spread of European core company (host) subsidiary base

	Africa	*Asia*	*Europe*	*LatAm*	*NorthAm*	*Oceania*	*TOT (host)*	*HERF*
1990	742	875	5527	763	1991	753	10650	0.326
1995	768	1179	5770	728	2051	683	11180	0.324
2001	289	1034	8943	637	2177	352	13432	0.479

The table shows that the overall concentration remained stable from 1990 to 1995, meaning all regions (except Latin America) grew proportionally. By 2001 Africa, and Oceania had dropped sharply, followed by both Latin America and Asia. Growth was found primarily in Europe, and secondarily in North America, leading to a rise in overall concentration (HERF = 0.479). These aggregates underscore the trends identified above and in previous sections: in the era of regionalism, European core companies focused firstly on their home regional base and secondly on North America as the locations in which to buttress their core positions.

8.1.3 Outside-in openness, Europe

In a world of inter-regional competition, it is not only the gravitational pull an RIA has on insider companies that matters. Its attraction for external actors is also crucial to determining the outcome of regional integration. Europe as a region was primarily concerned with the competitive position of European companies vis à vis their US competitors, which had established European beachheads long before the Single Market was born. The value of that European activity from 1990 through 1996-01 is shown in Table 8.2, along with the total number of subsidiaries held by the North American core set. The 'rest-of'-region' of European core companies is included for comparison.

Table 8.2: European activity of North American companies vs. Euro company 'rest-of-region' activity

	1990	*1991-95*	*1996-01*	*Slope 1*	*Slope 2*
Euro prod, NAF core companies	\$209.333	\$236.156	\$323.810	4.3%	8.2%
Euro prod (host), EU core companies	\$211.727	\$276.923	\$452.619	10.3%	12.3%
	1990	*1995*	*2001*	*Δ1*	*Δ2*
EU subs, NAF core companies	2144	2299	2768	7.2%	20.4%
EU subs (host), EU core companies	5381	5816	8186	8.1%	40.7%

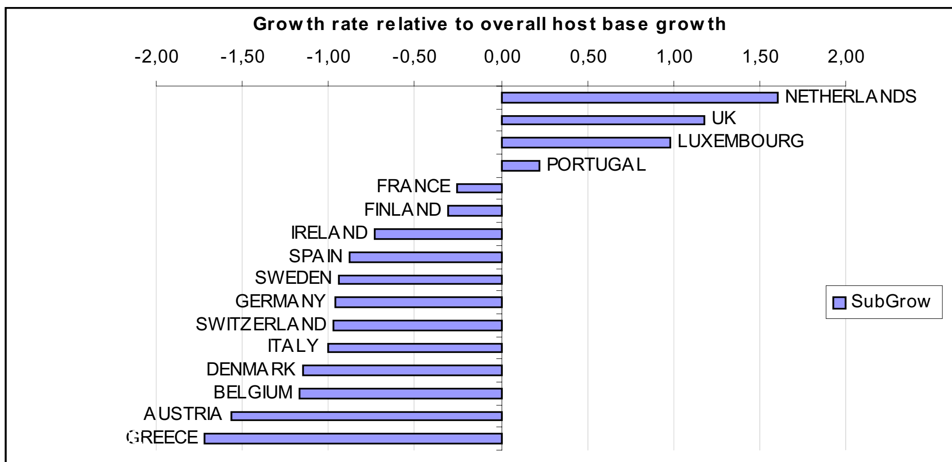
\$ values are US millions

The data show that on aggregate North American core companies held $209 billion in assets in Europe in 1990. This is in fact close to the $211 billion that European core companies held in other (host) European countries that same year. However, although production in the hands of US core companies rose on average over four percent per year from 1990 through 1995, the value for European core companies rose at a rate of ten percent, averaging $276 billion over the period. In 1996-01, the gap continued to grow. Although North American companies made considerable headway, doubling their growth rate to over eight percent, it was still less than the 12.3 percent growth rate shown by European core companies.

The trend in the development of their respective subsidiary bases is similar. Both subsidiary bases grew by 7 to 8 percent overall from 1990 to 1995; in the second period, however, the Europeans increased the size of their networks nearly twice as quickly as North Americans did. Since the question of openness is relative, the data clearly show that in terms of realized openness, European competitive space was considerably more open to European core companies, particularly after 1995, than it was to North American core companies.

To generate a sense of the distributive nature of North American penetration into the EU15 (+Switzerland), the formula in Figure 8.3 can be repeated (Figure 8.5). Here the average growth rate for the entire North American subsidiary base between 1995 and 2001 (26.7 percent) is taken as the baseline and the growth rates in individual companies are compared to that baseline.

Figure 8.5: Outside-in shifts in host subsidiary base (relative to average), Europe (1995-2001)



As for the European companies, the data show a pattern of a small number of host countries (the largest) which increased in importance from 1995 to 2001 (the Netherlands, the UK, Luxembourg and Portugal) and a larger number which grew in absolute terms (albeit more slowly) as well as a cluster whose subsidiary base actually contracted (Denmark, Belgium, Austria and Greece). Of those growing the fastest, it must be mentioned that Portugal and Luxembourg accounted together for just 60 subsidiaries in

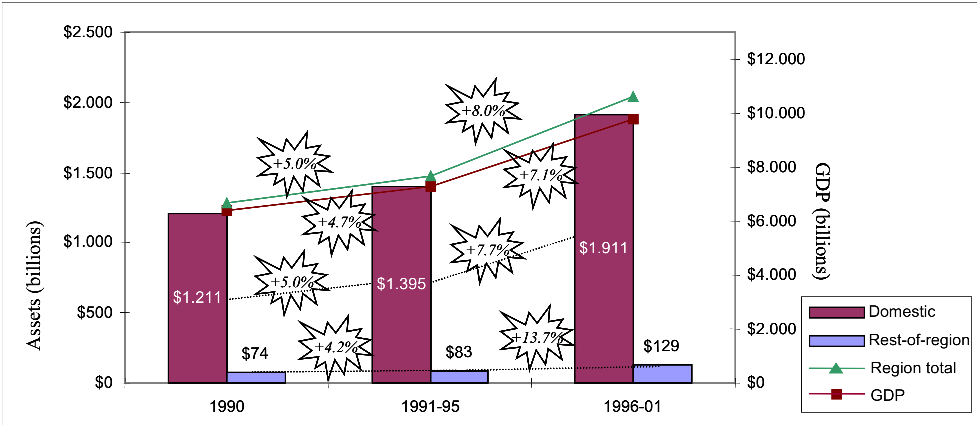
1995, whereas traditional investment destinations the UK and the Netherlands were the first and fourth largest host destination (respectively). The subsidiary base of North American core companies in Europe therefore shows a similar trend towards concentration as was the case for the European core companies.

8.2 Openness in North American competitive space

8.2.1 Inside-in openness, North America

Given that the NAFTA comprises only three countries, of which the United States forms the largest agglomeration of economic activity, the analysis is *de facto* one of US core companies and their internationalization into Mexico and Canada. Therefore where Figure 8.6 shows the aggregated domestic- and rest-of-region position for all 60 North American core companies (only one of which is Canadian and none Mexican), 'domestic' essentially stands for 'United States'.

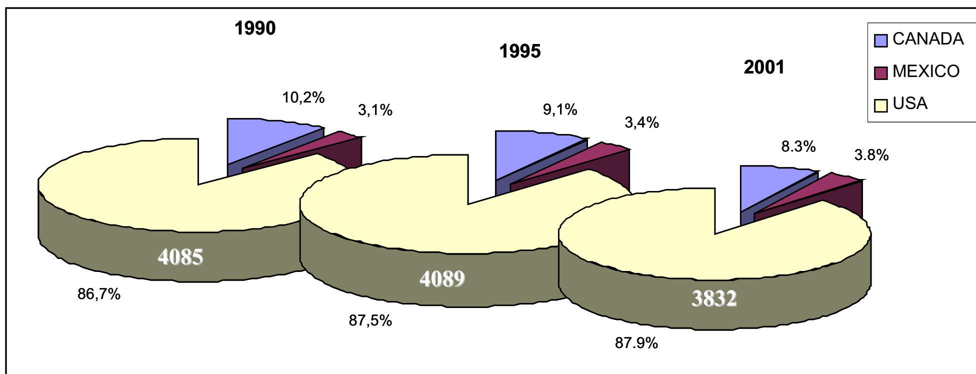
Figure 8.6: North American core company regional production (agg.) vs. NAFTA GDP



First, Figure 8.6 shows the absolute dollar values over time. Collectively, North American core companies controlled nearly $1.3 trillion in assets throughout the region in 1990. Over 1991-95 that figure averaged $1.5 trillion, and over 1996-01 it averaged over $2 trillion. Slopes over both periods closely parallel overall GDP growth, averaging 5.0 percent per year in nominal terms over the first period (compared to GDP's 4.7 percent) and 8.0 percent per year over the second (compared to GDP's 7.1 percent). Given the overwhelming proportion of domestic activity in the region as a whole, the aggregate domestic position follows total growth rates very closely. The rest-of-region value, initially very small ($74 billion in 1990), rose 4.2 percent over 1990-95, just slightly behind the overall growth rate. After 1995, however, the growth rate climbed to *13.7 percent*, to an average value of $129 billion over 1996-01. As a result, the value of activity in Canada and Mexico *as a share of total regional activity* held steady at about *six percent* over the decade.

Distribution of the regional subsidiary base can once again provide insight into the spread of activities within the region. Figure 8.7 shows three pie charts for 1990, 1995 and 2001, in which the aggregate regional subsidiary base of North American core companies is divided into respective shares for each of the three NAFTA countries. The data show that the overall subsidiary base contracted about three percent after 1995 whereas it remained constant in the previous period. As expected, the lion's share of the approximately four thousand subsidiaries was located in the US. That share, around 86 percent, actually showed a *very slight increase after 1995*, indicating that on average, the slight contraction in the total regional subsidiary base was not at the expense of the domestic share.

Figure 8.7: Inside-in network spread, North America (1990-2001)



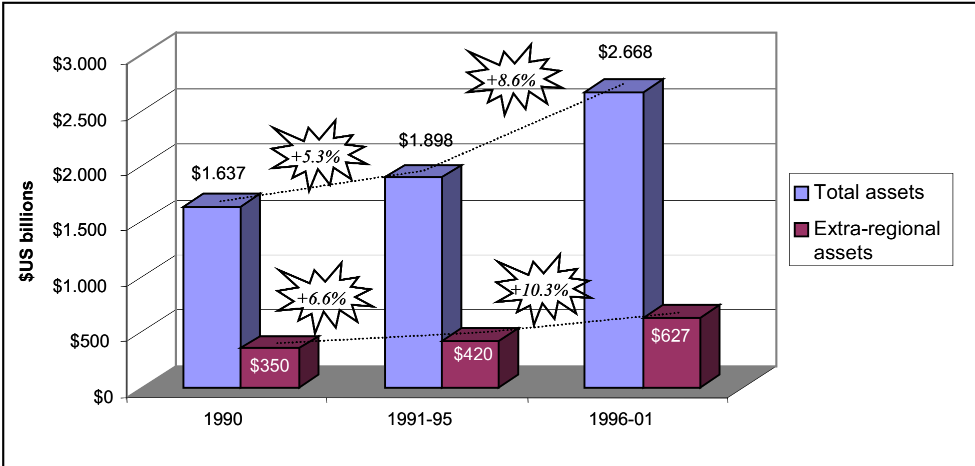
The majority of the shifts in the cumulative subsidiary base were experienced between Canada and Mexico. The Canadian share, at 10.2 percent in 1990, declined gradually to 8.3 percent in 2001 while the Mexican share showed the opposite trend, moving from 3.1 percent to 3.8 percent over the same period. Although these are not dramatic shifts at this aggregated level, in terms of the host country subsidiary bases they are symptomatic of a more significant impact. In terms of absolute number of subsidiaries, the Canadian base contracted by *ten percent* over 1990-1995 and another *fifteen percent* from 1995-2001. Conversely, the Mexican subsidiary base *grew* by ten percent over 1990-1995 and by an additional five percent over 1995-2001. To the extent that core companies lead internationalization processes, these shifts may be indicative of much larger-scale restructuring within the NAFTA region, apparently *at the expense of Canada and to the benefit of Mexico*. Overall, the *host* population of North American subsidiaries (excluding domestic subsidiaries), shrank from 526 in 1990 to 407 over 1991-95 and even further to 326 over the second period. This means the slope of decline was –7.5 percent over the first period and –1.4 percent over the second, translating into a relatively large reduction in the intra-regional host subsidiary base *prior* to 1995.

8.2.2 Inside-out openness, North America

Inside-out openness is measured in terms of the overall aggregated extra-regional position of North American core companies. Growth in the extra-regional value is juxtaposed

against growth in the total aggregate value of their assets to establish the extra-regional *share* of total activity (Figure 8.8). The figure shows once again that change in the aggregate, just as change for the average firm, was most pronounced in the second period. On aggregate, the total value of North American core company assets in 1990 was $1.6 trillion, nearly identical to the $1.5 trillion seen for European core companies above. Similarly, the aggregated extra-regional position was valued at $350 billion as compared to the $327 billion for European core companies. In fact both values follow the same pattern over time: in the first period, North American total climbed to $1.9 trillion and $2.6 trillion in the second, compared to $1.7 and $2.3 trillion for the European-based subset. The aggregate extra-regional position grew over both periods more rapidly than the total, but the shift was still more modest than that seen among European core companies (see above). From the $350 billion extra-regional position in 1990, that value climbed at a rate of over six percent in the first period to an average of $420 billion before reaching an average of $627 billion in the second period (compared to $373 and $684 billion for their European counterparts).

Figure 8.8: Aggregate value of extra-regional activity, North American core companies (1990-2001)



The aggregate extra-regional position of European core companies thus passed that of North American core companies in the course of the decade. This is at least in part a consequence of ownership changes under trans-Atlantic mergers and acquisitions, by which the initial 'insider' position of firms like Chrysler, Amoco and ARCO were transformed into 'extra-regional' activity of European core companies Daimler and BP. As a result, extra-regional activity, which accounted for 21.3 percent of the total in 1990, had climbed in the second period on average to only 23.5 percent (viz. 30 percent for European core companies).

The 'outside-in' position of North American core companies in Europe dealt with in the preceding section is a component of overall extra-regional activity as considered here. Linking the two provides insight into the *non-European* share of North American extra-regional activity. Of the $350 billion in extra-regional assets identified in Figure 8.8, only

$141 billion were located in other parts of the world besides Europe (40 percent of overall extra-regional activity and 8.6 percent of the total). By 1996-2001, that value had more than doubled to $303 billion, or 48 percent of overall extra-regional activity and 11.3 percent of the total. This shows once again that the modest inside-out expansion of North American core companies was aimed less and less at Europe.

The number of countries outside the region in which North American core companies operated fluctuated over the decade as well. Combined, they held majority-controlled subsidiaries in 103 non-NAFTA countries in 1990, of which nearly *half* (48) *had fewer than five subsidiaries*. In 1995, eight of these countries (all with only one subsidiary registered) no longer appeared in the aggregate North American core company network (such as Sudan, Kampuchea, Greenland and Lesotho). By 1995, 24 new countries were included in the aggregate subsidiary network, of which 16 were represented by only one subsidiary (very small countries such as Macao, Senegal, Yemen and the Faeroe Islands) and another eight had between two and four subsidiaries (in Eastern Europe, such as Slovenia and Bulgaria). Only two of the 24 newly included countries in 1995 (both in Eastern Europe) represented any substantial increase in the aggregate subsidiary network: Poland (22 subsidiaries) and the Czech Republic (21 subsidiaries). From the new total of 119 countries in 1995, 35 countries were no longer found in the data by 2001. Of these, the majority (21) were represented by only a single subsidiary, such as Tahiti, Togo, Gabon or St. Lucia, and only two had been represented by more than five subsidiaries in 1995 (Zambia and Liberia). In 2001, 17 new countries were included in the list, such as Estonia, Latvia, Albania, Lithuania, Iceland and Kazakhstan, bringing the total to 101.

Changes to the aggregate network over time reflect two major patterns. The first is the gradual opening of Eastern Europe in the mid-1990s and that of the former Soviet states in the late 1990s. The second is the sensitivity of the sample to fluctuations among a relatively large number of countries which account for a small fraction of the overall subsidiary base, in most cases represented by only a single subsidiary. Clustering the subsidiary data at a higher level of geographic aggregation (i.e., by geographic region) will help to compensate for some of this bias (Table 8.3). Recall that the HERF index used here is the spread of *host subsidiaries only*, that is excluding the position of domestic subsidiaries in their home countries.

Table 8.3: Geographic spread of North American core company (host) subsidiary base

	Africa	*Asia*	*Europe*	*LatAm*	*NorthAm*	*Oceania*	*TOT (host)*	*HERF*
1990	195	501	2.197	410	526	271	4.100	0.335
1995	203	581	2.429	407	487	294	4.401	0.349
2001	54	666	2.953	309	306	248	4.536	0.458

The table shows first of all the much smaller position of North America as a host region for North American core companies, due to the bias towards US companies. Secondly, the aggregate number of foreign subsidiaries of North American core companies is only a fraction of that of European companies which had a total foreign subsidiary base of 11 to 14 thousand over the decade (see preceding section). As a result, Europe is by far the largest host region, accounting for approximately half of all North American core company subsidiaries. Similar to the European case, Africa and Latin America show relatively sharp

declines after 1995 while Asia continues to host an ever larger number of North American-owned subsidiaries. The concentration index (HERF) for host subsidiary distribution follows in essence an identical trajectory as it did for subsidiaries of European core companies. The difference is that its rise does not reflect the proportionally larger share of the *home* region (which declines markedly as a share of the whole), but of Europe as *host* region. As the internationalization data showed, this must not be seen as part of a massive relocation to Europe. First of all, European subsidiaries are clearly much smaller than domestic subsidiaries. Secondly, the expansion is to some extent aimed at non-EU15 countries like the Czech Republic and Poland. Thirdly, there is a clear restructuring effort underway within the EU itself as the subsidiary base continues to concentrate in the larger and more Anglo-Saxon oriented countries, foremost in the UK, the Netherlands and Germany (see 8.1.1).

8.2.3 Outside-in openness, North America

The attraction of the North American market as a host location of outsider firms was one of the cornerstones of the North American Free Trade Agreement. The rules of origin, discussed in Chapter 5, were aimed at forcing producers targeting the North America market to locate their production within the region. Although much of this logic was aimed at low-cost Asian countries and Japan, Europe is the largest supplier of goods and investment to North America and hence the production decisions of its firms have a major impact on the outcome of the agreement as well. The value of North American activity of European core companies from 1990 through 1996-01 is shown in Table 8.4, along with the host activity of North American firms for comparison. The table also compares host subsidiary bases between the two regional subsets.

Table 8.4: European activity of North American companies vs. Euro company 'rest-of-region' activity

	1990	*1991-95*	*1996-01*	*Slope 1*	*Slope 2*
NAF prod, EU core companies	$197.166	$174.326	$321.628	-3,9%	26,3%
NAF prod (host), NAF core companies	$73.665	$82.852	$129.491	4,2%	13,7%
	1990	*1995*	*2001*	*Δ1*	*Δ2*
NAF subs, EU core companies	1991	2051	2177	1.0%	1.2%
NAF subs (host), NAF core companies	526	407	326	-7.5%	-1.4%

$ values are US millions

The data show that on aggregate European core companies held $197 billion in assets in North America in 1990. This cannot be directly compared to the intra-regional position of the North American firms because the latter excludes all US activity except for that of Canadian core company BCE. Since the US as an economy accounts for approximately 90 percent of NAFTA GDP (1995), it is likely that European core companies have the bulk of their assets in the US, such that the relative position of North American firms in Canada and Mexico is much greater.

The table also shows a drop in the aggregate value of European core firms' activity in North America from 1990 down to $174 billion in the first period. Yet the internationalization data have shown above that *as a percentage of the total*, North

America continued to grow slightly in the first period. Thus the drop in regional assets over 1990-95 shown in Table 8.4 is symptomatic of the total asset devaluation of European firms when translated to US dollars. But since the host position of North American companies rose during the same time (from $74 to $83 billion), the drop in value of European-held assets still means that their collective position was weakened in the region relative to that of North American companies. In that sense the changes after 1995 are all the more significant.

The rate of growth for the value of European-held assets in North America was twice as high as that for the value of North-American owned host-country assets (26 percent relative to 13 percent). The trend in subsidiary growth parallels that of the internationalization data: as the intra-regional host subsidiary base for North American companies experienced a gradual decline, the host subsidiary base of European core companies in North America continued to grow. Since the *domestic* subsidiary base of North American firms contracted as well, the result is an overall tipping of the scales in favor of European core companies. In 1990, North American companies had 4085 subsidiaries in the region (including domestic), while European core companies owned 1991 subsidiaries (49 percent). By 2001, the home-region subsidiary base of North American companies had contracted to 3832 while that of European core companies had grown to 2177 (57 percent). As a result, the overall balance between North American subsidiaries for North American companies and for European companies shifted in favor of Europe. The data show therefore that North America as a whole was increasingly open to European core companies after 1995.

The spread of subsidiaries throughout the region by country may shed some light on changes to the spread of outside-in activity within the NAFTA region. Table 8.5 shows the distribution of European-owned subsidiaries across the three NAFTA countries for 1990, 1995 and 2001. The three right-hand columns represent the subsidiary base of North American core companies in Canada and Mexico for the purpose of comparison.

Table 8.5: North American activity of European companies vs. home company 'rest-of-region' activity

	NAFTA subs of EU core companies			*NAFTA subs of US core companies**		
Host country	*1990*	*1995*	*2001*	*1990*	*1995*	*2001*
USA	1535	1605	1745	na	na	na
Canada	305	268	288	416	373	317
Mexico	150	158	144	127	140	147
	1990	**2031**	**2177**	**542**	**513**	**464**

*excluding domestic

As surmised above, the majority of the 'outside-in' subsidiary base is located in the US, with Canada second and Mexico third. Moreover, neither Canada nor Mexico demonstrates any clear trend, while the US grew undeniably as a host country over the decade. Note that the number of European owned subsidiaries in Canada and Mexico is comparable to that owned by North American companies: in 2001, European core companies owned 432 subsidiaries in Canada and Mexico, while North American core companies had 464. The outside-in spread of subsidiaries thus supports the conclusion that *the NAFTA as a region was relatively open to European core companies*.

8.3 Conclusions on the aggregate

The aggregate evidence strongly shows an opening up inside-in, both in absolute terms and more importantly, relative to the aggregate growth of the total activity controlled by European core companies, particularly in the period after 1995. More striking, however, is the role of extra-regional activity, which grew more rapidly than all other indicators. Moreover, North American core companies were clearly much less able to reinforce their European positions relative to European core companies although Europe was clearly a focus of growth. From this perspective, European competitive space can be characterized as most open from an inside-out perspective, then from an inside-in perspective, and only then from an outside-in perspective. In all likelihood the priority for European companies was to establish a platform from which they could resist pressure from their (North American) competitors freeing up resources for their own extra-regional expansion.

Aggregate home-region activity of North American and European core companies grew more rapidly than GDP. Although assets and GDP are not directly comparable, this may point to a concentration of activity within the region and thus power in the hands of (larger) core companies. This balance is particularly evident at the level of aggregate assets and also the even split in subsidiaries in Canada and Mexico between core companies from both regions. Europe tells a similar story but more one of subsidiaries than of aggregate value of activity. This is a reflection of the difference between micro- and macro-Fordism: in North America, subsidiaries are larger and there are fewer of them, while in Europe the subsidiaries are smaller and there are more of them. That is the result of the gravitational pull of bargaining partners under macro-Fordism versus the centralization of power under micro-Fordism.

In the 1990s, North America became increasingly inside-in open, but less so than Europe. The inside-in position of North American core companies grew over the decade such that the aggregate rest-of-region position remained stable despite its much smaller overall value. In terms of the intra-regional subsidiary base, an overall process of consolidation took place by which the increased value of output was spread over a shrinking subsidiary base. Within that contraction, there was a small but undeniable shift from Canada to Mexico. Inside-out North America was also less open, particularly as the pace of internationalization among core companies in general picked up in the second period. This was described in section 7.4 at the firm level, where numerous firms experienced a process of relative de-internationalization. The inward orientation of NAFTA (in part as a defensive measure in response to the EU) and the direct-control strategy of integrating North American operations can be considered a clear reflection of micro-Fordism and its inability to maintain global hegemony. The defensive position is consolidated in a regional hegemony.

Extra-regional expansion of North American core companies was proportionally less pronounced than that for their European counterparts, but at the same time it was relatively more aimed at the rest of the world outside of Europe as the main host region. This runs against the apparent role of Europe as the main focus of growth in the total North American-owned subsidiary base, suggesting that the growing number of subsidiaries in Europe was more part of a process of deeper embedding than a major organic expansion of productive capacity. Conversely, North America was increasingly inwardly open to European core companies (outside-in from the European perspective). The value of European-owned assets in the region grew more rapidly than intra-regional host-country

activity of North American core companies. Moreover, as the latter's subsidiary base in the region shrank, that of European core companies expanded. In Canada and Mexico, their respective aggregate subsidiary bases were more or less equal in size. From an outside-in perspective, North America became increasingly open to European firms and remained on aggregate more of a destination for European firms than Europe did for North American firms.

Aggregating core company activity by region of origin allows for certain conclusions as to the openness of European competitive space for European core companies and their North American counterparts. It must be recognized that aggregating company data allows for a greater sense of the overall (macro) impact of restructuring, but creates a major bias at the level of individual firm strategies. Since the largest firms in the sample are 20 to 30 times larger than the smallest firms, their role (and generally greater scale and scope of internationalization) distort the outcome. Therefore while the discussion centers on openness to 'firms', it actually refers to openness to assets (investment) while underplaying individual firm ownership of those assets. As a result the aggregated positions lead to different results than the strictly firm-based analysis in Chapter 7. This bias is an inherent element of the 'level of analysis problem'.

9. CONCLUSIONS

This study shows that core companies exhibited a wide range of strategic responses to the regionalizing institutional environment after 1995. Did core companies respond to regional integration in ways that policymakers expected? The short answer is that they did not, given the diversity they have shown in comparison to the relatively simple view of firm strategy one can distill from government policy models. This study hinged on the assumption that integration is more than just a trade agreement between government officials. The key actors in regional integration processes and outcomes are governments and firms, and integration is a phenomenon that involves the strategic visions and behavior of both types of actors. The differences between the strategic considerations governments face (strategic realities) and their plans for action (strategic intents) and those of firms created the potential for unexpected outcomes.

The answer to the second part of the leading research question of this study – what this implied for the nature, significance and viability of regional integration as a vehicle of international restructuring – is more complex. Regionalism has clearly eclipsed the multilateral system as the 'fast track' for international economic restructuring. With trade and investment talks within the WTO all but dead after the debacle at Cancun, a new 'regionalism' push – the 'Third Wave' – is in the offing as Europe prepares to welcome ten new members in May 2004 and the US seeks to consolidate its hemispheric hegemony in Latin America with the Free Trade of the Americas (FTAA) initiative. These two regions have emerged as the bi-polar core of the global economic system that not only govern a vast proportion of the world's economic activity, but also serve as role models to other nascent or fledgling regions. Their development over the past ten years shows that regionalism is very much alive. Moreover, the nascent 'Third Wave' of regionalism shows that tensions continue to exist between political strategies and core company strategies. For example, Western European companies are once again threatening to relocate as EU governments issue caps on labor migration from the new members.

The main conclusions will be grouped around the individual research questions posed in Chapter 1. Section 9.1 deals with the theoretical questions dealt with in Part 1 (Chapters 2 through 4). Section 9.2 focuses on synthesizing the empirical analyses and 9.3 discusses the ramifications of the results in the context of the broader debates on the relationship between regionalism and multilateralism, inter-regional competition and the crisis of post-Fordism. Section 9.4 introduces policy recommendations and Section 9.5 reviews the limitations of the study and suggests directions for future research.

9.1 Macro- and micro- dimensions of international restructuring

The first question to be investigated involved the search for 'missing links' in the literature:

1. *How is regional integration addressed in the traditional literature?*

In studying the mainstream literature on regional integration, three fundamental missing links came to light. First, a lack of attention for firm-level strategies with respect to regionalism; second, an overemphasis on intrinsic, efficiency-related arguments for integration and a tendency to downplay extrinsic, power-related motivations; and third, a

general failure to compare and contrast the rationale of government policymakers' intentions with the actual restructuring behavior of firms. Yet regionalism does not arise in a vacuum. A wide spectrum of policy motivations lies at its foundations. Moreover, these motivations hinge either implicitly or explicitly on expectations of firm responses to integration. The second research question addressed the way in which regionalism arises:

2. *What is the nature and the outcome of dynamic firm-government interaction in regional integration as a process of international restructuring?*

Companies, as the primary agents of economic restructuring, are the main actors involved in the actual economic restructuring in the wake of regional integration agreements (RIAs). Companies are not generic, however. Some companies lead restructuring processes through their size and financial muscle, their control of vital segments of the economy or their strategic positioning in (multiple) value chains. Perhaps more importantly, some companies have political vision as well as the access to political decision-makers by which to manifest that vision. These '*core companies*' straddle the political and economic divide, and form the linking pin between the macro-level reality of the policymaker and the micro-level reality of the firm.

Core companies, through lobby activity as well as the media, are often the standard bearers of regionalism and its benefits to society. This last point is crucial because the significance of regionalism rests in no small part on the assumption of its benefit to the societies of the countries it involves. Regionalism is 'sold' to the general public on the merits of arguments of societal gain for instance through dynamic growth, increased X-efficiencies and raised competitiveness. Most of these arguments, however, are based on highly abstract macro-realities that characterize policy decisions and the policy models that underlie them.

9.1.1 The 'muddled' macro-world of policy strategy

The first step in the analysis was to investigate the policy-level strategies behind regionalism. The policy level was dealt with first based on the assumption that regionalism is most easily understood as a political process and an economic outcome. The third research question read as follows:

3. *How can regional integration in its various forms be seen as a 'strategic repertoire' of policymaking behavior, or typology of geopolitical ambitions?*

A range of policy-level motivations for integration are described in the literature, such as domestic demand for reduced transaction costs (economic rationale); protectionism; a government strategy to pressure domestic stakeholders; an attempt to solve collective action problems at the inter-state level; as a form of 'defensible' multilateralism; or a naked strategy to maximize national power.

These visions are rooted in different notions of the relationship between actors at different levels: between states, between states and home companies, between states and host companies, and between states and civil society. Relationships are perceived as either harmonious or conflicting and governments, just as other actors, will try to manage their relationships and dependencies in such a way that they keep conflict at one or more levels

to a minimum. The policy outcome of regionalism represents the culmination of conflict minimization strategies, played out through bargaining processes at multiple levels.

The significance of regionalism is often juxtaposed against the background of the 'multilateral' system. Governments can adopt different positions in the 'multilateralism versus regionalism' debate, of which 'parallel regional multilateralism' is the most common. There are differences, however; while many European governments see regionalism as complementary to multilateralism, the US government is generally more pragmatic, opting for regionalism, multilateralism or even bi-lateralism depending on the circumstances.

Regionalism itself also has different meanings. In political terms, integration is first and foremost a matter of the *form* of integration, such as a Free Trade Area (FTA) or a Customs Union (CU). Integration is also described in terms of the depth or intensity of cooperation, the degree of 'legalization' or the balance of power between members. Economically, an RIA is judged in terms of its relative openness to trade and investment and thus whether it is trade- or investment- creating or diverting.

In dealing with these macro-level and geopolitical considerations, explicit understanding of the role of firms is often lacking. The perceived necessity of sweeping conclusions in order to 'sell' the agreement generates a reliance on highly abstract models in which the underlying assumptions of firm behavior are not even always clear. In reality, however, restructuring outcomes are contingent upon the behavior of individual firms, and core companies in particular.

9.1.2 Getting the firm out of the black box

Firms are strategic actors, not black boxes. Regional integration is designed to affect the strategies of firms, in particular with respect to their internationalization strategies and their organizational structures. The fourth research question dealt with the significance of regionalism for the strategies of core companies.

4. *What is the significance of regional integration for the spatial configuration and organizational structures of core companies?*

As strategic actors for whom their core positioning is in itself a strategic motivator, core companies face potential conflicts at different levels: with their value chain partners, with governments at home and abroad, and with other core companies. The risk of conflict creates a need for strategic response that involves not only intrinsic (efficiency- or cost-related) motives but also e.g. the reduction of conflict with certain actors. Core companies have various market- and non-market strategies they can apply to minimize conflict, such as increasing dependencies within their core complexes, threats of relocation or other actions that have direct negative impacts on governments, or even anti-competitive behavior towards other core companies ('gentleman's agreements').

Core companies are a heterogeneous group. They tend to owe their core status to their origins within the bargaining arenas of their home countries, and thus are identified in this study based on their home country – and more importantly, home region – origins. Core companies are also affiliated with different sectors, in practice straddling several sectors at the same time. Core companies involved in the automotive industry, for instance, tend also to be involved in industrial machinery or aerospace. Core companies involved in consumer

electronics are also often active in computers or scientific equipment. These *superclusters* are a more accurate representation of the differences and similarities among core companies.

These superclusters could also be divided into those that entailed activities with some degree of cross-border vertical integration and those without. The former are defined as having a *geographic division of labor*, by which production stages and production location are largely de-coupled from the location of demand. The latter are defined as *multidomestic*, by which an organization in essence replicates its strategy and control structure in individual national (and sometimes regional) markets, and in particular products are produced locally and tailored to local demands.

Most importantly, core companies represent a wide range of geographic profiles, described here in terms of *geographic scale and scope*. A typology of core company geographic profiles emerged in which the defining characteristic of strategy was regionality. Core companies can be domestically oriented, regionally oriented, bi-regionally oriented or globally oriented. The assumption was that internationalization strategies under regionalism would play out differently for core companies depending not only on the type of activity the company engages in (sector) or the characteristics of its home regional bargaining environment, but also its pre-existing spatial organization.

Regional integration is not only propagated on premises about company internationalization strategies, however. Arguments of efficiency, rationalization and consolidation also find expression in assumptions of changes to firms' organizational structure. Core companies may reduce the size of their subsidiary base, expand into new countries, or retreat from existing countries. They may develop deeper hierarchies within their host country network, or broaden their structures laterally to reflect e.g. a greater diversification in product portfolios.

9.1.3 'Openness' as a framework for macro-micro confrontation

As some have rightly pointed out, however, free trade agreements rarely involve free trade; 'the devil is in the details'. In keeping with the 'big picture' approach of the study, the assessment of regionalism from a policy perspective was based not on an in-depth analysis of specific details of individual articles, clauses and side-agreements in the European and North American RIAs. Instead, a framework was developed with which both the overall strategic intent behind regionalism strategies (particularly at the policy level) could be compared with realized restructuring outcomes in the strategies of core companies as an answer to the fifth research question:

5. *How can macro- and micro-strategic repertoires be compared and contrasted in a more comprehensive framework?*

The framework discusses regionalism origins and outcomes in terms of *openness*. Openness has two general dimensions, inward openness (intra-regional) and outward openness (extra-regional). Both dimensions also have two basic perspectives: from the inside and from the outside. This creates four angles to the discussion of openness (Figure 9.1): inside-in, outside-in, inside-out and outside-out. *Inside-in* openness refers to the propensity for region members to trade and invest intra-regionally. *Outside-in* openness is defined as the propensity for *outsiders*, or firms from other regions, to trade or invest in the

region in response to integration. *Inside-out* openness refers to the tendency for firms from inside the region to trade and invest more outside the region as a result of integration. *Outside-out* openness is one of the more underappreciated aspects of integration. It is in effect the 'systemic power' of an RIA to precipitate bandwagon behavior and increased openness among non-members. The openness framework in Figure 9.1 allows for a confrontation between the policy level rationale for integration (intent) and the realized restructuring behavior of core companies.

Figure 9.1: A framework for matching policy expectations with realized company restructuring strategies

	Inward dynamics		**Outward dynamics**	
	Inside-in	*Outside-in*	*Inside-out*	*Outside-out*
Policy orientation	← Policy intent? →			
Realized core company restructuring	← Core company restructuring? →			

9.2 A globalizing or regionalizing world?

The frame of reference for trade- and investment creation or diversion is, for all its flaws, the 'multilateral system'. From the policy perspective, an efficient and effective multilateral system is equated with 'globalization'. Unfortunately, one of the more short-sighted aspects of the debate is the wholly fictitious situation of 'global free trade'. A great deal of trade is not free at all, and free trade on a global scale has never existed and probably never will. Thus the comparison is based on deductive, theoretical consideration – some would call it 'pie-in-the-sky' thinking – which, despite its clear contribution to serious and inspiring scientific debate, clouds the reality of the issue. Part of the problem is that governments like to use the rhetoric of free trade and multilateralism when it suits their (sometimes short-term) goals. Even in more concrete policy environments like RIAs, policy-level restructuring is not very transparent and highly incomplete. Regional integration agreements can and do harbor 'rude surprises'.

9.2.1 Policy strategies for an integrated Europe and an integrated North America

The next research question addressed the strategic intent and reality of regionalism from the policy level.

6. *What strategic motives, and inherent assumptions of firm behavior, are evidenced in policy documents of the Single European Market (SEM) and North American Free Trade Agreement (NAFTA) as two prime examples of RIAs?*

A summary of the intended dynamics of regional integration in the SEM and the NAFTA is given below in Figure 9.2. The SEM was primarily an inward-looking solution to Europe's perceived problems of 'Eurosclerosis', segmented markets and low productivity. By opening up national markets to firms from other European countries (increased inside-in openness), greater competition and scale would provide opportunities for growth and lead to industry consolidation. The 'firm' in European policy models was quite clearly one forced to produce locally to circumvent tariff and other barriers which would naturally retreat to export servicing given the opportunity. At the same time it was expected that increased competitiveness among European firms would raise barriers to new entrants from outside the region (outside-in) or at least create stiffer competition for those outsiders already active in Europe. The gains from inside-in openness should also enhance the export competitiveness of European firms in extra-regional markets (inside-out) as well. In terms of outside-out openness, the European Union has always been more active in stimulating liberalization through multilateral channels than through integration itself. Still, it was understood that the systemic power of the world's leading RIA and fears of its exclusivity might lead to liberalization among outsider countries wishing to establish or maintain a preferential relationship with the EU.

Figure 9.2: The policy-level strategic intent behind the SEM and the NAFTA

	Inward dynamics		**Outward dynamics**	
RIA	*Inside-in*	*Outside-in*	*Inside-out*	*Outside-out*
Single European Market (SEM)	Concentration and consolidation: export replaces local production. Efficiency gains lead to virtuous cycles of growth and demand.	Raise entry barriers to outsiders through common external tariff and increased competitiveness of insider firms.	Increased overall competitiveness should lead to export competitiveness in extra-regional markets.	Not explicit in SEM; Multilateralism via WTO remained active.
North American Free Trade Agreement (NAFTA)	Greater regional division of labor consistent with patterns of comparative advantage. Rationalization of existing production.	Force outsiders to invest locally so that more of the gains from free trade and investment accrue to NAFTA countries. Insider firms still have 'home court advantage'.	Not explicit in NAFTA; outward dynamics governed by multilateral efforts at liberalization.	Force of integration to increase pace of liberalization in rest of world (Multilateralism).

The NAFTA was not only a shallower and less centralized integration effort, it was also more ideologically driven. The inward dynamics were focused on the ability of (primarily US) firms to establish regionally structured production networks based on comparative advantage in which access to Mexico as an intermediate production location played the key role. Outside in openness was aimed at investment, not trade, by forcing outsider firms to invest locally to meet rules of origin requirements. The need for local investment from the outside was in part a way to avoid using the cheapest point of entry as an export platform to the rest of NAFTA, but also a way to keep the US current account balanced. Inside-out openness in NAFTA played a subordinate and indirect role in combination with outside-out openness. The NAFTA was aimed at a consolidation of US hegemony in the region

through which leverage could be exercised upon other countries and regions as a strategy of ‘competitive liberalization’.
The intended dynamics of the two regions can be related to analyses of realized structuring behavior to evaluate the match between policy strategy and core company strategy. This leads to the final research question:

7. *What realized restructuring behavior do core companies exhibit in their spatial configuration and organizational structures under the SEM and NAFTA, respectively?*

This question was considered at different levels. Policymakers tend to use macro-level data (trade and investment) to analyze the outcomes of regionalism; therefore the analysis includes data at this level. To bring the firm out of its ‘black box’ and shed some light on ‘muddled’ macro-reality, however, the restructuring behavior of ‘real’ core companies was also analyzed. Finally, core company activity was studied at the aggregate level to try and bridge the gap between the macro and the micro. This complexity, and a desire to put the most salient conclusions ‘in the spotlight’ individually, necessitates a multi-stage response.

9.2.2 The second wave of regionalism and the bi-regional core

From the policymaker’s perspective, macro-level data are traditionally used to understand the outcomes of integration, despite the ‘muddled’ nature of such data. In terms of trade, the SEM and the NAFTA are (increasingly) inward-oriented. By comparison, the other three RIAs evaluated in the study (Mercosur, ASEAN and SADC) are all many times more outward-oriented in their export behavior. In the case of the SEM its inward orientation has existed at least since the mid-1980s, while the NAFTA only *became* relatively inward-oriented in the late 1990s.
As investors, the countries of the EU have turned slightly more inward in their orientation, with the growth in FDI stock increasingly aimed at other EU countries. The countries of the NAFTA region, however, are increasingly externally oriented as investors. But the interpretation of increased inside-out openness in the case of the NAFTA must be made with caution, since the US dominates regional investment and Canada and Mexico remain very small investment targets compared to the rest of the (extra-regional) world. In relation to their respective GDPs, inward investment stock from the US in Canada and Mexico has climbed dramatically over the second half of the 1990s.
The differences between the SEM and the NAFTA in this respect are in large part symptomatic of their different regional makeup. The EU is comprised of more countries, whose economies are more evenly balanced, while in the NAFTA the US is by far the largest market and largest investor. Since Canada and Mexico are so much smaller, and ‘foreign’ in the region is defined by only three borders, it is not surprising that the bulk of investment growth should be found outside the region. This does not detract from the fact that intra-regional trade and investment, relative to the size of the Canadian and Mexican economies, have increased dramatically.
The divergent strategies of North America and Europe are also evident in the multilateral dimension of their parallel regional multilateralism strategies, namely that of trade disputes before the WTO. EU and NAFTA countries are by far the chief litigants, and in a good many disputes their cases are aimed at one another. Some of the more high-profile trade cases have involved the export of (US-owned) Central American bananas to Europe and

the export of European steel to the US. In the first few years of the WTO, many of the disputes involving NAFTA countries were against other NAFTA countries. This has been less and less the case over time and as the North American RIA is consolidated, under the Bush administration in the US the atmosphere of *inter*-regional conflict has only increased. In fact the recent unilateralist tendency in US policy in general, and the 'twin deficit'-induced appreciation of the Euro, have been major factors in more recent European tendencies to 'look inward'.

If the veneer of multilateralism is peeled away, what remains are the origins of both regions as a strategic response to one another, in which regional core companies played a central role. Even as the US continues to try and assert itself as the world's only hegemon, the EU remains a force to be reckoned with. As geopolitical and geoeconomic forces, the EU and North America represent a formidable dyad, albeit one with a mix of harmonious and adversarial interests. Core company internationalization outside the bi-regional core is in all likelihood an attempt to establish a foothold in 'non-captive' competitive spaces.

These forces are creating a 'chasm' between these two regions, and an additional chasm between these regions and the rest of the world. The parallel regionalism–multilateralism strategy has thus far amounted to 'having the cake and eating it too'. Trade with the US and Europe is far from free and far from a level playing field for other countries. More importantly, the increasingly central role played by these two regions in the world economy is only making the playing field less level, akin to a concentration of economic power (duopoly) on a global scale. Only very recently have other parts of the world been able to find the strength in numbers to start bargaining more as equals, such as the banding together of twenty two developing countries at the WTO negotiations in Cancun in 2003.

One of the reasons regionalism among developing countries such as the Southern African Development Community (SADC) or the Mercado Común del Sur (Mercosur) in Latin America has failed to deliver on the promise of prosperity is because the playing field is not level. Only for a very select group of countries with sufficient leverage does 'going it alone' appear to remain viable, such as China, India or the Russian Federation. For the bulk of the world's nations, the second wave of regionalism is facilitating a 'chasm' between the dyad of North America and Europe on the one hand, and the rest of the world on the other.

9.2.3 Regionalism, the 'global' hype and the bi-regional chasm

The globalization debate has its micro-level counterpart in the myth of the 'global firm'. In the 1990s, 'going global' was all the rage, even though being global was never very clearly defined. Its persistence is in part a result of its ambiguity. In reality, the pervasiveness of the 'global firm' rarely lives up to the hype. The analysis in Chapters 6 and 7 of the spatial organization of the North American and European core companies clearly demonstrates that 'global' is a predicate that (still) can only be reserved for only the select few.

On average, core companies had more domestic activity than foreign activity. Even at the beginning of the new millennium, the average degree of internationalization among the largest core firms was 36 percent and only a quarter of their activity was located outside the home region. The regional aspect was clearly at the core of the dynamic of core company restructuring but also the dynamics *between* core companies. Regionally oriented companies, for instance, were several times more likely than core companies with any other geographic orientation to be acquired at the hands of other core companies. In most

cases, this also involved acquisitions by core companies from the same region. Consolidation was therefore also evident among firms and not just within firms.

Compared directly, extra-regional growth was greater than intra-regional growth. However, if the difference in size between the home region and the rest of the world is taken into consideration, intra-regional growth was relatively more important. More critically, the *pace of internationalization accelerated after 1995*, *and the acceleration was intra-regional*. Meanwhile the number of host countries increased *prior to* 1995, which suggests shallow explorative internationalization prior to regional integration and a subsequent deepening of host-country networks afterwards.

European and North American core companies in most cases did not primarily target each other's region as the locus for expansion; in fact their 'second region' positions tended to decline over the decade (more so for US core companies). Sales in the second region, however, grew more rapidly than production in the second region. That suggests that production is increasingly replacing sales in increasingly peripheral (extra-regional) locations. Such a gradual outward expansion of first sales followed by production, in effect increasing the geographic scope of activity, is suggestive of a bi-polar core (North America and Europe) complemented by an extra-regional periphery. Concomitantly, sales growth is substituting for production growth in the second region.

While these developments underscore the trend towards consolidation of a bi-regional core, it does not indicate that 'bi-regionalism' is the core company strategy of choice. This is because the relationship between the two regions in the bi-regional core is one of conflict, while a bi-regional strategy at the firm level is only possible if some degree of harmonization is possible. The increased polarization between the two regions had as a result that of all strategy types, the bi-regional strategy appeared particularly ill-suited to the second wave of regionalism.

9.3 The political economy of regionalism

Integration in both regions has its similarities and core companies from both regions demonstrate to some extent comparable strategic migrations. But processes and outcomes in both regions can be contrasted as well. In evaluating the differences between European and North American integration, the analysis also provides a stepping stone towards broader conclusions on the significance and viability of regionalism as a vehicle for international restructuring in general.

9.3.1 European integration versus North American integration

Policy strategies differed between Europe and North America in both the policy measures and the expectations of firms. Figure 9.3 summarizes the macro-micro confrontation for the SEM and the NAFTA, respectively. For each of the three dimensions of openness addressed in the study a conclusion is given as to the degree to which the strategic intent at the policy level matched realized restructuring outcomes at the firm level.

Inside-in, European integration has led more to an intra-regional expansion of production than consolidation within home countries and export to the rest of Europe. In the meantime their North American competitors have shifted their focus away from Europe to some extent. Clearly, the intended reduction in outside-in openness has been successful. Overall, therefore, restructuring has led to a greater prominence of European core companies in the

European economy (in some countries more than others). In the process, European core companies became larger and – from a bargaining perspective – have gained in strength primarily through size and industry concentration. European core companies also internationalized inside-out over the decade, often even producing in other regions to supply European markets. In this sense European companies may have become more efficient, but it is not clear whether this has increased competition and thus growth in the region. It seems more likely that these changes have led to gains through decreased competition and a greater concentration of market power among core companies.

Figure 9.3: Matching macro-intent and micro-realities, SEM and NAFTA

	Inward dynamics		**Outward dynamics**	
	Inside-in	*Outside-in*	*Inside-out*	*Outside-out*
SEM	– – Extensive intra-regional cross penetration instead of retreat and 'clearing out' European competitive space	+/– EU presence of US MNEs reduced. Still, efficiency gains from consolidation may have been better reaped by US core companies.	+/– Supply leakage of production as core companies seek new extra-regional bases from which to bolster core positioning.	Not investigated
NAFTA	++ Greater regional division of labor consistent with patterns of comparative advantage. Rationalization of existing production.	++ Outsiders forced to invest locally so that more of the gains from free trade and investment accrue to NAFTA countries. Insider firms still have 'home court advantage'.	+ Split in competitive space. Either clear regional focus, or extra-regional focus. Options, and competitive space, are clearer.	Not investigated

In the NAFTA countries, restructuring has centered largely on the US and Mexico as an improved regional division of labor was established. In many cases this involved actual de-internationalization, in others a general shift in focus to the region. This has not, however, signaled a general retreat to 'isolationist' positioning as consolidation within the region has allowed in particular regionally oriented core companies to expand extra-regionally as well. Core companies with higher internationalization levels, however, have been particularly strong in retreating not only to the home region, but in particular to the home country, suggesting that North American regionalism exerts a gravitational pull in particular on core companies with 'overstretch'.

The rigid adherence of the EU to parallel regional-multilateralism is perhaps less hypocritical than the relatively opportunistic US approach to international negotiations, but is also a handicap and in particular potentially debilitating for European core companies. This is not to say that a 'mismatch' between intended and realized outcomes is a negative qualification of integration. For core companies in the European setting the 'cluttering' of European competitive space may have been necessary to maintain their core positions in the shift from national to regional oligopolies, but was clearly not the outcome envisioned by European governments. Thus *ex post* the evidence supports earlier suspicions that European core companies and European governments may have both had a vision of integration, but for different reasons.

Integration in North America has arguably been more 'brazen', and subject to significantly lower levels of strategic 'disconnect' between (US) core companies and (the US) government, which has in turn made it less hypocritical. This had in part to do with the pluralist character of the EU versus the hegemonial character of the NAFTA. In the case of the EU, a greater number of countries took part in policy formulation, each with potentially divergent interests despite the shared vision of regional integration (as an abstraction). Moreover, each country in Europe is home to its own base of core companies, with their potentially divergent interests with respect to e.g. nationally segmented markets. The NAFTA, on the other hand, revolves around the interests of a relatively coherent group of US-based core companies. The NAFTA also has less of a 'human face'; despite the pro-NAFTA public relations campaign in the early 1990s, the agreement is still seen by most as a 'gift' to US core companies and not a tool for socioeconomic improvement.

European governments continue to carry the 'burden' of social policies that in the eyes of many European core companies were largely the *reason* for integration in the first place. As the European Union prepares to expand east in May 2004, why have nearly all EU member governments agreed to caps on labor migration from Central and Eastern Europe? To protect the welfare state. To this European core companies say 'if they can't come here, we'll go there', which sounds eerily reminiscent of the threats made prior to the Single European Act in 1986. This may be the legacy of European bargaining environments; European core companies may be less able to be honest in their interactions with policymakers. The cost of Europe's social face may be disjointed communication between business and government that leads to 'muddled' outcomes.

9.3.2 The crisis of post-Fordism

The relationship between regionalism outcomes and the characteristics of European and North American bargaining environments links the analysis to the power struggle between the EU and NAFTA in the context of post-Fordist crisis. It can be argued that the efficiency motives behind integration, in the form of e.g. a smaller subsidiary base, are more easily realized in a micro-Fordist environment. The evidence shows that the typically macro-Fordist environment of European core companies is characterized by a much larger subsidiary base, reflecting the 'stickiness' of the European bargaining environment. That stickiness is a major component of the problem of 'Eurosclerosis' which the SEM was intended to combat. Over time, European core company subsidiary networks have grown, particularly intra-regionally, which suggests a greater degree of interpenetration, but not necessarily the consolidation and efficiency gain which the SEM was purported to entail.

From the perspective of the 'selling points' of integration, North America has come closer. Despite popular opposition to the agreement, the NAFTA seems to be a success (from the perspective of its proponents). Intra-regional activity has grown dramatically, both in terms of general trade and core company restructuring. Subsidiary bases have been streamlined, reducing the 'drag' which cumbersome networks create and which are symptomatic of business activity in Europe. The NAFTA has been a boon mostly to vertically integrated core companies with a solid regional position (such as General Motors, Ford and Chrysler) with an increased regional division of labor, which also explains why the NAFTA became inwardly oriented in trade in the late 1990s. The NAFTA has served as the motor behind the establishment of a regional base within which to bolster the waning micro-Fordist concept of control and thus reestablish American hegemony. This is also evident in the

greater tendency of the more highly internationalized North American core companies to retreat over the 1990s. As the gravitational forces of both regions increase, the ‘chasm’ makes in particular the direct control strategies of North American bi-regional companies less tenable as strategic vision becomes too incoherent and overall coordination is disrupted.

9.3.3 The viability of regionalism

North American integration may be more successful in that its outcomes better reflect its strategic origins. Economic logic, and even the superficial evidence of prosperity over the second half of the 1990s, would suggest this is a gain to society. But it remains unclear if this has led to more equality and ‘social justice’ in terms of the welfare gap between rich and poor, or between Mexico and Canada on the one hand and the US as regional hegemon on the other. That issue remains hotly debated both in society and among the experts (see e.g. the debate between Mexican and US trade economists in Foreign Policy, September / October 2002).

Additionally, society seems to react more skeptically to shallower forms of integration like the NAFTA than to deeper forms like the European Union. This is perhaps due to the perception that shallow integration serves primarily corporate interests by oiling the wheels of commerce without a clear sense among the general public that they will themselves benefit from any gains that might derive from integration (despite high-intensity government campaigns to that effect). Deeper integration is associated with not only *de*-regulation (negative integration), but also with *increased* regulation at other levels (positive integration). In this way the public sees corporate interests as bound to some extent by the fact that governments also make concessions in their own bargaining power and room to maneuver for the sake of the region as a whole.

Integration agreements such as the NAFTA and its potential successor the FTAA are unlikely to serve as *permanent* alternatives to a true multilateral order (i.e., one not dominated by a relatively small number of large and powerful Western ‘core’ countries). Regionalism is also a form of ‘defensible multilateralism’ for firms, which are themselves primarily regional in nature and of whom only a select few have the geographic scope to exercise true global systemic power. A parallel regional-multilateral strategy will only succeed as a sustainable, viable strategy in the long term if the two strategies are convergent in their objectives. Similarly, parallel regional-multilateralism will fail unless countries pursuing that strategy (the US and EU members foremost among them) do not make more of an effort to level the playing field for other countries via the multilateral system. The EU and the NAFTA have a role model function to fulfill; in that sense their attitudes towards sustainable, equitable open regionalism will be crucial to fostering similar integration elsewhere as ‘building blocs’ of a sustainable, equitable multilateral system.

9.4 Policy recommendations

The observations and conclusions of this study lead to a number of policy recommendations. First and foremost, the need to understand the ‘big picture’ at the macro level should not come at the expense of the micro level. It is important to recognize that there are different kinds of firms, whose strategies are shaped by concerns that cannot be

reduced to simple efficiency-related or welfare-enhancing motives or even to the level of sectoral dynamics. Core companies need more attention, not just in the lobby arena, but also as the leading economic actors which largely determine restructuring outcomes, directly and indirectly. Moreover, the fact that firms express a 'shared strategic vision' similar to that of policymakers does not mean they hold that vision for the same reasons. Fiat did not support market integration because they were hoping for more competition in the Italian car market and the inevitable loss of market share; Fiat (and many others) supported integration hoping to rationalize their supply chains and gain from increased competition between, and scale opportunities for, their suppliers; in addition, the company hoped to keep foreign competitors – in particular Japanese car producers – out of its home turf through European policies rather than through national policies. Other core companies adopted a pro-Europe stance on the basis of simple 'herding' behavior, i.e. following the competition in order not to be left behind.

These are legitimate strategic considerations, albeit ones based on extrinsic motives and the preservation of core positioning. These dimensions are lacking in policy models, which tend to be a poor estimate of core company behavior because e.g. price signals are not always transmitted effectively and also because price signals, production frontiers, market structure and elasticities are certainly not the only factors core positioning is based upon. In addition to the real-world shroud of uncertainty surrounding such variables, core companies (and governments for that matter) are also unlikely to reveal their cards fully in any up-front bargaining processes. Bargaining is a complex process for which it should be assumed, or at least considered, that interests will continue to conflict even if an agreement is reached.

Still, 'tidy' models based on such variables tend to be the mainstay of policy analysis. This is not to say they are not useful, because such models do establish parameters within which outcomes are likely to play out. But in isolation they create the risk of self-fulfilling prophecy when 'businessmen parrot economic theory' based on the 'bright side' of expected firm behavior. This applies particularly to smaller, non-core players that are not in an adequate position to know what the stakes of integration are. The result may be a shift in (market-, bargaining) power towards core companies and away from other smaller stakeholders. International restructuring is, after all, a 'small numbers game' in which the rules are set at least as much on the basis of extrinsic, strategic considerations as on the basis of intrinsic, economically rational ones.

The firm is not a black box. If the variation among firms is taken beyond strict sectoral lines firm-level responses can be analyzed perhaps less rigorously, but more accurately. Moreover, the baseline needs to be taken into account. What is the firm's pre-existing spatial organization strategy? Is its strategy based on a cross-border division of labor, or on (semi)autonomous multidomestic bases? What strategic considerations emerge on the basis of that 'strategic reality' and how do they translate into 'strategic intent' with respect to regional integration? These are feedback loops of strategic positioning and migration that set the stage for future core company restructuring.

Restructuring can be thought of at different levels. In this study the consequences of restructuring were considered in terms of 'openness', which itself has different dimensions. Regional integration is not only a matter of changing 'inside-in' openness (and indirectly outside-in); it has ramifications for restructuring from the inside-out as well as outside-out. Considering the impact of restructuring on openness means understanding not only the strategic reality and intent of core companies, but also the positioning strategy of the

government itself and thus how institution-building at the regional level is intended to fit into the wider multilateral world.
Making regionalism a viable strategy within multilateralism requires more effort to 'level the playing field' with respect to in particular developing countries. If the inherent difficulties developing countries incur in accessing regional markets and the externally imposed barriers to climbing the value-added ladder are institutionalized through regional integration agreements, regionalism will never be a multilateral building 'bloc'. In doing so Europe and the NAFTA, as the world's flagship regions, will deliver the 'wrong' message to developing countries and reinforce their suspicions of inequity. The specter of multilateral collapse in this context has been seen at WTO meetings in Seattle, Doha and Cancun, and the risks are high.
Assuming democracy works, governments will be held accountable for the policy decisions they take. Regionalism may be actively 'sold' on the wrong premises, it may lead to unexpected outcomes or it may simply fail to deliver what was promised. In each case, governments, policy think tanks or academia may present the 'muddy' macro-reality of regionalism as 'proof' of the positive outcomes. A 'match' between macro intentions and micro realities is not necessarily positive if integration was portrayed differently and civil society perceives that match as a 'conspiracy' between government and 'big business'. The NAFTA 'gone wrong' as a theme in the 2004 Democratic campaign for the US presidency is demonstrative of the lack of social embeddedness of integration in North America; in Canada and Mexico these feelings are even stronger.

9.5 Limitations and directions for future research

This study has contributed to an improved view of the dynamic process of regional institution-building as a vehicle for international company restructuring by focusing on the potential tension between governments and core companies. By emphasizing the feedback loops between strategic reality, strategic intent and realized restructuring strategies, the stage is set for a small numbers' game of perception and misperception. Governments and firms do not share the same strategic intent and strategic reality, and thus macro (policy) intentions do not always play out as micro (company strategy) realities.
The existing bias towards intrinsic (rational, economic efficiency oriented) motivations in the literature on regional integration has been complemented with extrinsic (power-based) motives that center on power relationships between stakeholders. These extrinsic issues translate into strategies by which core companies and governments try to manage conflict at multiple levels to preserve their position within the international 'oligopolistic' structures in which they operate and compete. In analyzing these issues, the study has explicated government positioning- and internationalization strategies as dimensions of unilateralism, regionalism and multilateralism.
At the same time core company positioning- and internationalization strategies have been explicated as consisting of vertical- and horizontal positioning within the value chain, the scale and scope of internationalization, and the level of cross-border coordination. Moreover, the study contributes organizational and network spread dimensions to give the discussion on core company strategies more depth. This has generated an appealing typology of strategy that not only allows for the identification of existing strategy (static), but also allows for strategy 'migration' over time.

The 'openness' framework presented here provides a convincing means to analyze strategic intent and realized restructuring at both the macro- and the micro level. This framework forms not only a bridge between levels of analysis but also, through its 'inward' and two 'outward' dimensions, the link between regionalism and multilateralism. In doing so the study unravels the tangled traditional macro-understanding of regionalism and international restructuring more generally. Finally, the study provides conclusive evidence that globalization, despite its 'mass appeal', is reserved only for the 'happy' few.

These contributions still leave plenty of room for future research. For instance, no performance indicators have been taken into account to identify whether regionalism seems to have led to higher profits or larger market shares. It has also for example not yet been established whether European core companies have actually become more competitive or whether the creation of a European competitive space has amounted to regional protectionism.

Future research is also needed to supplement the analysis of openness with the 'outside-out' dimension. For instance, the internationalization strategies of Japanese core companies over the same period would shed considerable light on the impact of regionalism on outsiders. Although others have contributed work on Japanese internationalization in Europe in anticipation of 'Fortress Europe' after 1992 and on their capitalization of gains through NAFTA, research is needed to investigate their restructuring strategies in particular in Asia, and thus their efforts to secure their value chains outside of existing RIAs.

In trying to bridge the gap between the macro and the micro, the study risks criticism for addressing neither level with complete adequacy. It was, however, deemed more important to 'set the stage' of debate through this study and leave room for more in-depth research in the future, for instance at the case level of individual firms as well as investigating in much more detail changes to backward- and forward linkages at the empirical level. The same applies to *horizontal* linkages *between* core companies, through e.g. joint ventures or cooperation agreements.

A much larger sample of firms would also allow for the possibility of statistical relationships between e.g. asset distribution and FDI stocks. Macro, for that matter, clearly represents a wider range of sectors than those identified in this study; services, for instance, represent a larger share of value added than manufacturing. Although their core positioning is derived from different variables, core companies in services would be a welcome addition.

Similarly, the study might be criticized for not identifying an explicit 'RIA effect'. This can be countered on the basis of three arguments. Firstly, a major assumption of the study is that economic (or political) actors are not fully rational actors and thus do not respond to 'exogenous' policy as a behavioral 'switch'. Secondly, the study explicitly takes a holistic approach by which no effort is made to isolate a region which is only one part of the world economy, or only one part of a firm's strategy, and that is inextricably intertwined with the rest. Thirdly, the option of interviews with firm strategists has many risks, foremost among them the potential for 'PR spin' given the ten to fifteen years of hindsight and the fact that many of the individuals from the relevant time period (late 1980s – early 1990s) would be difficult to trace. Additionally, given the conscious choice to build a bridge between the macro and the micro, in-depth case studies would likely have been too specific and too far removed from the broader context. Clearly, however, it would be worthwhile to use this study as a backdrop for future interviews with policymakers and with core companies.

APPENDICES

Appendix I: The SCOPE Core200

ID #	Company name	Country	ID #	Company name	Country
1	Mitsubishi Corporation	Japan	57	Samsung Corporation	South Korea
2	Mitsui & Co., Ltd.	Japan	58	Kmart Corporation	United States
3	Itochu Corporation	Japan	59	ABB Asea Brown Boveri Ltd	Switzerland
4	General Motors Corporation	United States	60	The Procter & Gamble Company	United States
5	Sumitomo Corporation	Japan	61	The Daiei, Inc.	Japan
6	Marubeni Corporation	Japan	62	Peugeot S. A.	France
7	Ford Motor Company	United States	63	Vivendi	France
8	Toyota Motor Corporation	Japan	64	BASF A.G.	Germany
9	Exxon Corporation	United States	65	Bayerische Motoren Werke AG	Germany
10	Royal Dutch/Shell Group**	Netherlands	66	Alcatel S.A.*	France
11	Nissho Iwai Corporation	Japan	67	Chevron Corporation	United States
12	Wal-Mart Stores, Inc.	United States	68	Hewlett-Packard Company	United States
13	Hitachi, Ltd.	Japan	69	Mitsubishi Heavy Industries, Ltd.	Japan
14	Nippon Telegraph & Telephone Corp.	Japan	70	Bayer AG	Germany
15	AT&T Corp.	United States	71	Nippon Steel Corporation	Japan
16	Daimler Benz A.G.	Germany	72	PepsiCo, Inc.	United States
17	International Business Machines Corp.	United States	73	Ito-Yokado Co., Ltd.	Japan
18	Matsushita Electric Industrial Co., Ltd.	Japan	74	France Télécom SA	France
19	General Electric Company (GE)	United States	75	VIAG Aktiengesellschaft*	Germany
20	Tomen Corporation	Japan	76	Carrefour	France
21	Mobil Corporation*	United States	77	Thyssen Krupp AG	Germany
22	Nissan Motor Co., Ltd.	Japan	78	Amoco Corporation*	United States
23	Volkswagen AG	Germany	79	Total Fina S.A.	France
24	Siemens AG	Germany	80	Motorola, Inc.	United States
25	BP (Amoco)	UK	81	The Kansai Electric Power Co., Inc.	Japan
26	Metro AG	Switz/Ger	82	Petroleos de Venezuela, S.A.	Venezuela
27	United States Postal Service (USPS)	United States	83	East Japan Railway Company	Japan
28	Chrysler Corporation*	United States	84	Ssangyong Corporation	South Korea
29	Philip Morris Companies Inc.	United States	85	Nippon Mitsubishi Oil Corporation	Japan
30	Toshiba Corporation	Japan	86	Robert Bosch GmbH	Germany
31	The Tokyo Electric Power Co., Inc.	Japan	87	SK (Sunkyong)	South Korea
32	Daewoo Corporation	South Korea	88	Samsung Electronics Co., Ltd.	South Korea
33	Nichimen Corporation	Japan	89	ConAgra, Inc.	United States
34	Kanematsu Corporation	Japan	90	British American Tobacco p.l.c.	UK
35	Unilever N.V./ Unilever PLC**	Netherlands	91	AB Volvo	Sweden
36	Nestlé S.A.	Switzerland	92	The Kroger Company	United States
37	Sony Corporation	Japan	93	Dayton Hudson Corporation	United States
38	Fiat S.p.A.	Italy	94	Hyundai Corp.	South Korea
39	Veba AG	Germany	95	Canon Inc.	Japan
40	Deutsche Telekom AG	Germany	96	Lockheed Martin Corporation	United States
41	NEC Corporation	Japan	97	United Technologies Corporation	United States
42	Honda Motor Co., Ltd.	Japan	98	British Telecommunications PLC	UK
43	Elf Aquitaine*	France	99	Japan Postal Service	Japan
44	Electricite De France (EDF)	France	100	Mannesmann AG*	Germany
45	Istituto Por La Ricostruzione Industriale	Italy	101	Pemex (Petróleos Mexicanos)	Mexico
46	Royal Philips Electronics	Netherlands	102	Enel SPA	Italy
47	Fujitsu Limited	Japan	103	Jusco Co., Ltd.	Japan
48	E.I. du Pont de Nemours and Company	United States	104	Chubu Electric Power Co., Inc.	Japan
49	RWE Group	Germany	105	J.C. Penney Company, Inc.	United States
50	Renault	France	106	Suez Lyonnaise des Eaux	France
51	Texaco Inc.*	United States	107	United Parcel Service of America	United States
52	Mitsubishi Motors Corporation	Japan	108	The Dow Chemical Company	United States
53	Hoechst Aktiengesellschaft	Germany	109	Deutsche Bahn AG	Germany
54	ENI S.p.A.	Italy	110	Japan Tobacco Inc.	Japan
55	Mitsubishi Electric Corporation	Japan	111	Promodès S.A.*	France
56	Sears, Roebuck and Co.	United States	112	GTE Corporation	United States

113	International Paper Company	United States	157	Petrõleo Brasiliero S.A.	Brazil
114	J. Sainsbury plc	UK	158	Electrolux AB	Sweden
115	Taisei Corporation	Japan	159	Imperial Chemical Industries Plc	UK
116	The Boeing Company	United States	160	Intel Corporation	United States
117	Mazda Motor Corporation	Japan	161	SHV Holdings N.V.	Netherlands
118	Tesco PLC	UK	162	Minnesota Mining & Manufacturing	United States
119	Xerox Corporation	United States	163	Compart Spa.	Italy
120	Shimizu Corporation	Japan	164	Caterpillar, Inc.	United States
121	Johnson & Johnson	United States	165	Nabisco Group Holdings	United States
122	Preussag AG	Germany	166	Groupe Danone	France
123	NKK Corporation	Japan	167	Tohoku Electric Power Co., Inc.	Japan
124	Sanyo Electric Co., Ltd.	Japan	168	Japan Energy Corporation	Japan
125	Koninklijke Ahold	Netherlands	169	Usinor	France
126	American Stores Company (Albertson's)*	United States	170	Pechiney	France
127	Kajima Corporation	Japan	171	Pinault-Printemps-Redoute	France
128	Costco Companies, Inc.	United States	172	The Home Depot, Inc.	United States
129	USX Corporation	United States	173	Btr Plc.*	UK
130	The Coca-Cola Company	United States	174	Takenaka Corporation	Japan
131	BCE Inc.	Canada	175	Kobe Steel Ltd.	Japan
132	Bridgestone Corporation	Japan	176	Eastman Kodak Company	United States
133	BellSouth Corporation	United States	177	MCI WorldCom, Inc.	United States
134	Nippon Express Co., Ltd.	Japan	178	Repsol S.A.	Spain
135	Mycal Corporation (Nichii)	Japan	179	Federated Department Stores, Inc.	United States
136	Sara Lee Corporation	United States	180	Japan Airlines Company, Ltd.	Japan
137	Columbia/HCA Healthcare Corp.	United States	181	UAL Corporation	United States
138	Novartis Group*	Switzerland	182	Sumitomo Metal Industries, Ltd.	Japan
139	Fleming Companies, Inc.	United States	183	Kyushu Electric Power Co., Inc.	Japan
140	Deutsche Post AG	Germany	184	Bouygues	France
141	Isuzu Motors Limited	Japan	185	Compaq Computer Corporation	United States
142	RAG Aktiengesellschaft	Germany	186	Idemitsu Kosan Co., Ltd.	Japan
143	Sociedad Estatal De Part. Industriales	Spain	187	Denso Corporation	Japan
144	Sharp Corporation	Japan	188	Thomson SA	France
145	Mitsubishi Chemical Corporation	Japan	189	AlliedSignal Inc. (Honeywell)*	United States
146	Rhône-Poulenc	France	190	McDonnel Douglas*	United States
147	Toyota Tsusho Corporation	Japan	191	Suzuki Motor Corporation	Japan
148	AMR Corporation	United States	192	Georgia-Pacific Corporation	United States
149	Franz Haniel & Cie. GmbH	Germany	193	Saint-Gobain	France
150	Karstadt Group	Germany	194	Kawasho Corporation	Japan
151	Atlantic Richfield Company (ARCO)*	United States	195	Telefonaktiebolaget LM Ericsson	Sweden
152	Merck & Co., Inc.	United States	196	Telefónica S.A.	Spain
153	La Poste	France	197	Deutsche Lufthansa AG	Germany
154	Supervalu Inc.	United States	198	Sekisui House, Ltd.	Japan
155	Fried Krupp AG*	Germany	199	Dentsu Inc.	Japan
156	Safeway Inc.	United States	200	Digital Equipment Corporation*	United States

Notes

* subject to merger or acquisition during the 1990s

** Dual nationality (British / Dutch)

Appendix II: Sales, asset and subsidiary reporting in the SCOPE database

Many large and publicly traded firms include a geographic segmentation in their annual reports which lists all or some combination of these three indicators for the various geographic regions in which the firm is active. Accounting standards allow firms to report geographic regions based on their own circumstances as opposed to a standardized taxonomy. At the same time, accounting standards differ by country, with Anglo-Saxon countries exhibiting strong similarities, most continental European countries exhibiting similarities of their own, and Japanese accounting standards forming yet another distinct structure (Daniels and Radebaugh, 2001). In most accounting regimes firms are required to disclose geographic segment information (as well as line-of-business segments) if foreign *revenues, assets or profits* are at least 10 percent of corporate total (Qian & Li, 1998: 159). In general, geographic regions are required to reflect materially different business environments in terms of e.g. 'proximity, economic affinity, similarities in business environments and the nature, scale and degree of interrelationship of the enterprise's operations in the various countries' (SFAS 14, cited in Nobes and Parker, 1998) or e.g. return on investment (ROI), risk, growth, or future growth potential (SSAP 25). In addition, they should be consistent with those reported by 'other companies', and be consistent over time. Since these three characteristics can be conflicting, it is generally up to companies to determine which should be most prominent.
In addition to the accumulation of pure quantitative data, studying the way firms segment their activities geographically is in itself also a research outcome in that it reveals how firms themselves perceive the geography of their production. The research project, built around the SCOPE database (Studies and Competence Centre for Organizational and Policy Research in European Business), also exposes the methodological hazards faced while putting together the database and collecting quantitative data of this nature. Although data were initially drawn from secondary sources, it soon became evident that data collection, and the calculations of 'foreignness', were not always executed consistently across sources, much less across firms or over time. As a result, the indicators described above showed erratic patterns which could not be explained by e.g. divestment, mergers or exchange rate fluctuations alone. In the analysis of data from 200 companies (the 'Core200') over a ten-year period in the form of 2,000 annual reports (complemented with 10-K forms), four major pitfalls presented themselves that formed the root of the discrepancies: 1) Random use of sales by origin and sales by destination; 2) Random allocation of 'eliminations'; and 3) Random allocation of geographically unspecified data

IIa: Geographic segment reporting in the SCOPE database

In order to illustrate the diversity of reporting styles, we have analyzed the core 200 for the 10-year period 1990-1999. Table IIa shows how many of the Core200 reported geographic segment data for sales, assets and employment over the period (irrespective of definition). The 'eligible' *n* reflects the number of companies in the Core200 for which geographic segment data can be expected.

Table IIa: Data reporting among the Core200, 1990-1999

	1990	*1991*	*1992*	*1993*	*1994*	*1995*	*1996*	*1997*	*1998*	*1999*
Eligible *n*	160	160	160	161	162	167	169	168	167	164
Sales	112	114	121	130	136	145	147	149	140	136
Assets	65	65	65	71	73	98	98	102	98	97
Employment	49	48	47	51	56	62	60	61	62	52

There are multiple reasons why 30-40 companies of the Core200 fall outside the eligible *n* per year. Firstly, as accounting regulations change (or the general corporate attitude towards disclosure), companies may change their reporting procedures. In fact, regulations in many countries were relaxed from 1997 onward (requiring less disclosure), a fact immediately evidenced by the post-1996 reporting drop in all three variables. Secondly, the number of core companies in the initial sample is reduced over the period by a total of 7 due to mergers and acquisitions that occurred in the course of the decade. Thirdly, some companies were not required to report (e.g. as a consequence of not being not publicly listed), or are highly secretive or otherwise not forthcoming with data of this nature (e.g. South Korean chaebols). Fourthly, some members of the Core200 are domestic-only and thus not subject to geographic segmentation requirements. Although this sub-set declined over the period, by 1999 22 core companies still qualified as 'wholly domestic'. As others internationalized over the decade, they became subject to reporting requirements and subsequently 'joined' the sample.

'Reporting' in Table IIa is defined at any level of geographic segmentation, varying from 'foreign vs. domestic' to the specification of activities in as many as 20 individual countries. Striking is the disparity between reporting of the three indicators. Different indicators generate different *n*s because only rarely do companies report all three variables. Sales is the most common, while employment is relatively rare. In general, reluctance to report (beyond the level required by accounting standards) is related to the perceived sensitivity of the information. Additionally, there is variation within firms over time, as firms do on occasion switch from e.g. sales-only reporting to sales and asset-reporting.

IIb: Subsidiary location data, Dun & Bradstreet

In practice, sales, asset and employment data are available at the level of geographic (and sometimes political) regions (i.e., the 'geographic segments' identified in company annual reports), but rarely at the level of individual countries. Data on the location of a company's subsidiaries can provide more insight into the breakdown of activities across geographic regions. Moreover, the two indicator types are to a certain extent complementary: while a sales etc. give an indication of a geographic segment's relative importance, they say little about the role of individual countries within the segment; and while subsidiary location says a great deal about the place of different countries in a company's network, it says little about that country's relative importance (or indeed that of the individual subsidiary itself).

Dun and Bradstreet (D&B) is an agency which maintains continuously updated records on the activities of companies worldwide for the purpose of issuing credit reports to parties interested in conducting business with companies in the D&B database. These data have been structured in the 'Who Owns Whom' database, containing the 'family trees' of thousands of the world's largest companies. The family tree consists of the global ultimate parent (GUP, e.g. 'Ford Motor Corp.') and various types of companies which fall under that parent. Originally subsidiaries were described as full subsidiaries (at least 50%

ownership), affiliates (less than 50% ownership), trade investments (no controlling shares) and dormant (no registered economic activity). Each subsidiary (where relevant) has in turn its own subsidiaries, and so on, such that a 'tree' is formed (only the subsidiaries of majority-controlled subsidiaries are included, generating a great variety of hierarchical depth. The corporate tree of BTR, for instance, was comprised of subsidiaries at 14 levels in 1990, while e.g. all of Compaq's subsidiaries were first-level subsidiaries. Each subsidiary is registered according to the country in which it is legally incorporated. The family trees are published annually in book form (and more recently on CD-ROM) in several volumes corresponding to geographic regions (e.g. Great Britain and Ireland, Continental Europe, North America, Australasia). The CD-ROM and on-line accessed versions of the database contain additional information per subsidiary where available (sales, employment, SIC-codes). While forming a treasure trove of information, the D&B data are subject to serious methodological considerations.

Firstly, it is not always clear where the data were drawn from and whether the data are complete. D&B claims to purchase their data from 'every Chamber of Commerce around the world' (i.e., where firms are required to register their activities) yet serious discrepancies have emerged between the D&B data and e.g. the lists of company subsidiaries in their annual reports and 10-K forms. It is unclear at this time whether there are Chambers of Commerce with which D&B does *not* have purchasing agreements. It is therefore difficult to verify whether the data reflect *complete* corporate trees or not.

This discrepancy can also be related to two other issues: firstly, D&B no longer includes minority-controlled subsidiaries in its database; therefore the discrepancies between subsidiaries reported by companies themselves and those noted by D&B may conceivably be attributed entirely to this omission (in by far the most cases, companies themselves reported a greater number of subsidiaries than D&B). The analytical implications of these omission is likely to be an understatement of the role of developing countries in a given company's network, since developing countries are more likely to have investment provisions restricting majority control by foreign companies. In 1990, for instance, the Core200 had subsidiaries in ca. 160 countries, of which more than 100 could be qualified as 'developing'. For their entire collective base of more than 31,000 subsidiaries, 17.7 percent were minority-controlled (5500). In developing countries, that percentage climbed (based on aggregate values) to 28 percent while the figure for developed countries was 16.6 percent. It is possible that this discrepancy has been reduced or eliminated over time as e.g. investment provisions converge worldwide (see 1995??), but we can't say…

More fundamentally, however, is the distinction between *legal* location and *physical* location. Since D&B registers companies and their subsidiaries by country of legal incorporation, that does not always imply that the company is physically present in that country. In practice this usually means subsidiaries physically located abroad are registered in the home country for reasons of e.g. legal liability. As a consequence, internationalization measures based on D&B data are likely to understate fact, and again, this is likely to have a disproportionate bearing on the weight of developing countries in a given analysis.

Similarly, subsidiary location, whether only legal or in fact physical, does not always indicate productive activities. In 1990, for example, the Dutch Antilles were 30th in the list of countries with most subsidiaries registered on its territory. It can, however, easily be surmised that the vast majority of those subsidiaries have a financial function and not a productive one. For this reason subsidiaries in locations such as the Cayman Islands,

Bermuda and the Dutch Antilles were omitted in order to minimize bias in the geographic spread of production.

Finally, the legal nature of the D&B database's origins also poses the question whether a legal relationship is in any way translates into an economic relationship. In terms of hierarchy, for instance, the depth of (legal) relationships, or the vertical vs horizontal characteristics of a corporate tree, is used as a proxy for the required level of coordination, particularly where those relationships are across borders. Yet it is hypothetically possible that those 'vertical' relationships are in no way related to e.g. trade relations between subsidiaries. Still, it seems intuitively likely (unless all the vertical relationships refer to trade investments, where in fact no control is exercised) that a complex vertical, cross-border legal structure would entail a greater effort to coordinate than e.g. a shallow organization in which all subsidiaries answer (legally) directly to the ultimate parent. Moreover, an obvious explanation for a complex legal structure in the absence of complex economic and strategic relationsips is not in evidence.

Appendix III: Methods for manipulating the key variables

Data collection on the geographic segmentation of the three indicators form an integral part of research conducted since 1997 at the Erasmus University of Rotterdam to document the internationalization patterns and behavior of the world's 200 largest (non-financial) companies over the 1990s, measured by value of total sales in US dollars in 1995 (see Van Tulder *et al*., 2001). In addition to the accumulation of pure quantitative data, studying the way firms segment their activities geographically is in itself also a research outcome in that it reveals how firms themselves perceive the geography of their production. The research project, built around the SCOPE database (Studies and Competence Centre for Organizational and Policy Research in European Business), also exposes the methodological hazards faced while putting together the database and collecting quantitative data of this nature. Although data were initially drawn from secondary sources, it soon became evident that data collection, and the calculations of 'foreignness', were not always executed consistently across sources, much less across firms or over time. As a result, the indicators described above showed erratic patterns which could not be explained by e.g. divestment, mergers or exchange rate fluctuations alone. In the analysis of data from 200 companies (the 'Core200') over a ten-year period in the form of 2,000 annual reports (complemented with 10-K forms), three major pitfalls presented themselves that formed the root of the discrepancies: 1) random use of sales by origin and sales by destination; 2) random allocation of 'eliminations'; and 3) random allocation of geographically unspecified data. The current section explores the significance and extent of these issues and offers methodological tools through which they can be addressed consistently and systematically, based on the research in the SCOPE database.

IIIa: Sales by origin and sales by destination

A company's sales can be defined either by *origin* or by *destination*. Sales by origin (SO) are equal to the sum of net sales (gross sales minus value added taxes and similar levies) generated from subsidiaries in a certain location, while sales by destination (SD) are equal to the sum of net sales (gross sales minus value added taxes and similar levies) generated from subsidiaries in the location in question *plus* sales imported from the headquarters or subsidiaries in other countries (Van Tulder *et al*., 2001). The former definition is also applied by Worldscope (Worldscope data definitions guide: p. 213) but excludes excise taxes, windfall profit taxes, value added taxes (VAT) and general and services taxes (GST). In the US, UK and Dutch accounting standards, for example, companies are required to publish both sales by origin and sales by destination, 'unless the two are not materially different' (Nobes and Parker, 1998).

For many companies and certain sectors more generally, the two will not be 'materially different' if, for example, a company sources all its inputs locally. Each type of sales has a common denominator in terms of e.g. market share or the attributability of sales to production within a particular location or to a specific division of management. Furthermore, each says something different about the importance of the location to that company in general, and equally importantly, the significance of the company for the location. For industries which exhibit vertical integration across widely dispersed locations such as the automobile industry, the difference can be quite remarkable. For Daimler-Benz

in 1995, for instance, foreign sales by origin (FSO) accounted for 45.6 percent of the total, while the figure for foreign sales by destination (FSD) was 63.2 percent (a difference of 17.6 percent). Canon, in the same year, exhibited FSO of 64.1 percent and FSD of 66.9 percent (a difference of 2.8 percent). In some cases the differences may seem minor or insignificant, but it should be noted that for these indicators, a two percent change year-on-year is considerable, even in large firms (cf. Muller and Van Tulder, 2002). It is vital that 'fluctuations' in internationalization indicators are not attributable to random use of these variables. When comparing the significance for a company of a given location, particularly within industries, it must be clear which type of sales figure is being used. Moreover, this type should ideally be used consistently across firms, but in any case for individual firms over time.

Table IIIa illustrates the significance of the problem. Theoretically, companies have three possibilities: reporting SO, SD or BOTH. The data show that, of the three options, SO is by far the most frequently reported, outscoring SD by a ratio of about five to one. The figure also reveals an increased tendency to report BOTH over the decade, rising from only 7 percent of those firms reporting geographically segmented sales in 1990 to a high of over 20 percent in 1996 before tapering off again in the late 1990s. Since firms are only required to report both if 'materially different', the rise in BOTH may reflect an increasing geographic diversification in production and marketing structures.

Table IIIa: Sales reporting, 1990-99 Core200

	1990	*1991*	*1992*	*1993*	*1994*	*1995*	*1996*	*1997*	*1998*	*1999*
Total N	112	114	121	130	136	145	147	149	140	136
% BOTH	7,1	7,0	9,1	11,5	15,4	18,6	20,4	18,1	17,9	15,4
% SO	79,5	78,9	78,5	78,5	75,0	72,4	71,4	69,8	67,1	69,1
% SD	13,4	14,0	12,4	10,0	9,6	9,0	8,2	12,1	15,0	15,4

If reporting only SO or SD suggests that the difference is immaterial, they can in theory be used interchangeably. However, since a considerable number of firms disclosing geographically segmented sales data report BOTH, the sales type must be selected which most accurately reflects the concept it is intended to measure, and that consistency over time is maintained.

IIIb: Calculating shares based on geographic sales data

The calculation of a geographic segment's relative importance as a percentage of the whole seems at first glance rather straightforward. For any company X, it is logical to express the share of any segment *i*, as a share of the total, as follows:

$$Share_{iX} = \frac{Sales_{iX}}{Sales_{TotalX}} \quad \text{(Equation 1)}$$

where $Share_{iX}$ is expressed as a percentage.

When reporting revenues data, however, companies often include some form of eliminations in alongside the geographic segment data. Eliminations generally refer to intra-firm sales, or intermediate goods that are consumed in the production process and must be accounted for in the balance in such a way that they are not re-counted at each

stage in the production process (list also in Appendix?). 'Unallocables' refer to a geographically unspecified item in the geographic sales data that does NOT represent eliminations or other references to intra-firm sales (e.g. 'incidental', 'miscellaneous', 'associated undertakings'). The problem with eliminations and unallocables is that they can influence the calculation of a company's geographic spread depending on how they are included in the calculation. This is because many companies list an aggregate eliminations figure as opposed to specifying eliminations per region. Non-elimination unallocables, for their part, are never geographically specified. In calculating percentages based on segment data which include either an aggregate eliminations figure or an otherwise unallocable sum, one runs the risk of allowing that value to function as a region of its own in the percentages.

Table IIIb addresses the complex issue of eliminations and other unallocables reported along with the geographic segmentation of sales data. The Total N row refers to the number of companies reporting eliminations and / or other geographically unspecified sales figures at any time during the decade. In general the list comprises only companies reporting SO, because SD by nature refers to sales to external customers and is thus a net (post-eliminations) figure.

Table IIIb: Sales reporting among the Core200, 1990-1999

	1990	*1991*	*1992*	*1993*	*1994*	*1995*	*1996*	*1997*	*1998*	*1999*
Total N	104	104	104	104	104	104	104	104	104	104
No data	24	25	21	10	8	4	5	3	10	12
Elim by region	34	37	40	50	54	58	62	58	33	29
No elim/unall	20	17	18	17	16	14	15	18	41	39
Elim Aggregate	20	21	19	19	18	21	17	18	13	14
Unallocable other	3	2	4	5	6	7	5	6	7	9
Other	3	2	2	3	2	0	0	1	0	1

The first row ('No data') shows how many of the 104 firms reported no data for that year. This high figure in the early 1990s is largely due to the cluster of firms not engaged in cross-border activity at that time (i.e., domestic firms), while the rise at the end of the 1990s most likely reflects changes in accounting regimes. In fact, all figures change considerably after 1997 such that the later period should be considered somewhat in isolation. In some cases firms for specific years were subject to data collection problems due to annual report unavailability. It is important to recognize that individual firms 'migrate' between rows over time, moving from 'no data' one year, to geographically specified eliminations another year and aggregate eliminations for yet another. That being said, firms do exhibit a certain level of consistency over time in this respect, each changing their sales reporting style on average about 1.5 times in the course of the decade.

In general there was a trend towards increased reporting, and at a higher level of detail. An increasing number of firms, for example, specified their eliminations by geographic segment ('Elim by region') over the period while the number reporting eliminations only as an aggregate declined ('Elim Aggregate'). This allows for post-eliminations segment sales being taken as a share of post-eliminations total sales, thereby circumventing the 'allocability' problem. Until 1998, an additional 20 to 25 percent of the firms did not report any eliminations or otherwise unspecified segment data.

The ‘Unallocable other’ row refers to the number of firms reporting a geographically unspecified item in their geographic sales data that does NOT represent eliminations or other references to intra-firm sales (e.g. ‘incidental’, ‘miscellaneous’, ‘associated undertakings’). The last row (‘other’) comprises a small number of firms reporting a geographically unspecified (unallocable) item in *addition* to eliminations, be they specified or not. Both ‘Unallocable other’ and ‘other’, together with ‘Elim Aggregate’, require methodological interventions in order to prevent the eliminations and otherwise geographically unspecified value from skewing the percentages. These three categories taken together consist of 20 to 30 percent of the firms reporting in any given year.
Example 5.2 below describes such a case, drawing on Motorola in 1998 (based on data provided in the 1999 annual report, page 30). Following Equation 1, $Share_{USMotorola}$ in example 5.2 = 20,397 / 29,398, or **69.4 percent**. However, calculating $Share_{USMotorola}$ based on $Sales_{TotalMotorola}$ as listed on the balance sheet implicitly allocates the eliminations figure (-9,520) to the other segments; i.e., to segments *other* than $Sales_{USMotorola}$.

Example 1: Aggregate eliminations in geographic segment reporting: Motorola, 1998

Geographic segment	*Sales (millions $US)*
United States	20,397
United Kingdom	5,709
Other nations	12,812
Adjustments and eliminations	-9,520
Total	**29,398**

Companies do on occasion segment their eliminations (intra-firm sales) by region as well, which allows for analysis of net revenues per segment. Since geographic segment data reported as in Example 1, however, provides no information as to the proper segmentation of the eliminations figure, there is no theoretical basis for allocating the eliminations to other segments, or any segment for that matter. Given that fact, a methodologically sounder (arguably still imperfect) calculation would be as follows:

$$Share_{iX} = \frac{Sales_{iX}}{Sales_{TotalX} - Sales_{ElmnationX}} \qquad \text{(Equation 2)}$$

The calculation for Motorola (1998) is then 20,397 / (29,398- [-9,520]), or **52.4 percent**, or a difference of **17 percent**. The comparison of a *pre*-eliminations segment total with a *pre*-eliminations company total is more accurate than comparing a *pre*-eliminations segment total with a *post*-eliminations company total. Although it may be more desireable to have *post*-eliminations segment totals, the reality of firm reporting is often otherwise (see following section). Moreover, in practice, the *absolute* value of eliminations when aggregated as in Example 1 will often be *higher* than the value of one or more individual geographic segments and can thus create a margin of error greater than the value of a small segment (e.g., if the absolute value of the eliminations is higher than the absolute value of a given segment).

Since in practice, it turns out that some companies report more than one unallocable figure, or an eliminations and an unallocable in the same geographic segment overview, a more generally applicable calculation method for sales follows in Equation 3:

$$Share_{iX} = \frac{Sales_{iX}}{Sales_{TotalX} - \sum_{1}^{n} Sales_{UndefX}} \qquad \text{(Equation 3)}$$

where ‘Undef’ (1…*n*) equals all unsegmented eliminations, miscellaneous or otherwise geographically unspecified items in the geographic segmentation.

IIIc: Calculating shares based on geographic asset data

Unallocable categories in the geographic segment data are quite similar in fact to the eliminations categories, except that they more often relate to assets and not sales figures. Examples of unallocable are e.g. ‘corporate assets’, ‘associated undertakings’, and ‘corporate items’.
Table IIIc is analagous to Table IIIb in that it demonstrates the problem of unallocables with respect to assets. The issue is considerably less complex than for sales since firms never specify such additional assets per region nor report more than one figure per year. As with sales, no trend is evident that spans the decade in its entirety. Up through 1997, the number of firms reporting assets, and the number of firms reporting unallocable asset values rose in conjunction. Of those companies reporting geographically segmented asset data, anywhere from half to two-thirds will include some geographically unspecified asset figure. This higher proportion can be interpreted as a higher risk of error in the calculation of regional asset shares.

Table IIIc: Unallocable asset reporting, 1990-99, Core200

	1990	*1991*	*1992*	*1993*	*1994*	*1995*	*1996*	*1997*	*1998*	*1999*
# reporting assets	65	65	65	71	73	98	98	102	98	97
# with unallocables	40	37	39	39	42	63	61	62	35	37
Percentage	61,5	56,9	60,0	54,9	57,5	64,3	62,2	60,8	35,7	38,1

As with eliminations, such unallocable or geographically undefined categories can influence the calculation of a company’s geographic dispersion and skew the apparent relative significance of a given geographic segment. So just as one may erroneously compare the total for a segment *i* with the total on the balance sheet (as in Equation 1), a more appropriate measure would be the calculation in Equation 2, modified for this case.

$$Share_{iX} = \frac{Assets_{iX}}{Assets_{TotalX} - Assets_{UnallocableX}}$$

Example 2 below demonstrates the problem for ARCO, using the data from 1990 (drawn from the 1991 annual report, page 44).

Example 2: Unallocable assets in geographic segment reporting: ARCO, 1990

Geographic segment	*Identifiable assets (millions $US)*
United States	18,744
Canada	5,031
Europe	2,139
Other foreign	2,995
Unallocated corporate	3,244
Total	**31,765**

Calculating $Share_{USArco}$ in example 2 based on Equation 1 gives 18,744 / 31,765, or **59.0 percent**. However, calculating $Share_{USArco}$ based on Equation 2 gives 18,744 / (31,765-[3,244]), or **65.7 percent** – a considerable difference.

However logical these arguments may seem, closer examination will reveal the prevalence in International Business research of FA and FS percentages calculated using Equation 1. The methodological shortcomings of Equation 1 only become glaringly apparent when percentages are calculated for *all* geographic segments, and then tallied. Depending on whether one is faced with a negative number (e.g., eliminations) or a positive number (e.g., corporate assets), the sum of all percentages will either be more than 100 percent or less than 100 percent, respectively. Since most studies addressing firm-level internationalization are only concerned with the foreign-domestic dichotomy, this fact is easily overlooked through the calculation of a percentage based on one segment alone. Note that *absolute* values generated from these percentages will not accurately reflect the 'real' value of sales or assets; the procedure is applied to the calculation of *relative shares* only.

REFERENCES

Aglietti, Michel. 1979. *A Theory of Capitalist Regulation: the US Experience*. London: NLB.

Aharoni, Yair. 1966. *The Foreign Investment Decision Process*. Boston: HBS.

Alt, James and John T. Woolley. 1982. Reaction Functions, Optimization and Politics: Modelling the Political Economy of Macroeconomic Policy. *American Journal of Political Science*, vol. 26(4): 709-740.

Andersson, U. And Johansson, J. 1997. International Business Enterprise. In: I. Björkman and M. Forsgren, eds., *The Nature of the International Firm*. Copenhagen: Handelshøjskolans Förlag.

Annavarula, Madan & Sam Beldona. 2000. Multinationality-Performance Relationship: a Review and Reconceptualization. *International Journal of Organizational Analysis*. 8 (1): 48-67.

Aristotelous, Kyriacos & Stilanos Fountas. 1996. An Empirical Analysis of Inward FDI Flows in the EU with Emphasis on the Market Enlargement Hypothesis. *Journal of Common Market Studies*, 34(4): 571-83.

Arthur, W. Brian. 1989. Competing Technologies, Increasing Returns and Lock-in by Historical Events. *The Economic Journal*, 99(394): 116-31.

Athanassiou, Nicolas & Douglas Nigh. 2002. The Impact of the Top Management Team's International Business Experience on the Firm's Internationalization: Social Networks at Work. *Management International Review*, 42(2): 157-81.

Atkinson, Glen. 1999. Developing Global Institutions: Lessons to be Learned from Regional Integration Experiences. *Journal of Economic Issues*, 33(2): 335-44.

Baden-Fuller, Charles & Gianni Lorenzoni. 1995. Creating a Strategic Centre to Manage a Web of Partners. *The California Management Review* 37(3): 146-163.

Bakker, Isabella & Riel Miller. 1996. Escape from Fordism: the Emergence of Alternative Forms of State Administration and Output. In: R. Boyer & D. Drache, editors, *States Against Markets: the Limits of Globalization*. London: Routledge.

Balanyá, Belen, Ann Doherty, Olivier Hoedeman, Adam Ma'anit & Erik Wesselius. 2000. *Europe, Inc.: Regional and Global Restructuring and the Rise of Corporate Power*. London: Pluto Press.

Balassa, Bela. 1961. *The Theory of Economic Integration*. Homewood, Il: Richard D. Irwin.

Baldwin, Richard. The Growth Effects of 1992. *Economic Policy* 9: 247-81.

Baldwin, Robert. 1985. *The Political Economy of US Import Policy*. Cambridge: MIT Press.

Baldwin, Robert. 1996. The Political Economy of Trade Policy: Integrating the Perspectives of Economists and Political Scientists. In R. Feenstra, G. Grossman & D. Irwin, editors, *The Political Economy of Trade Policy*. London: MIT Press.

Baldwin, Robert. 1999. Agglomeration and Endogenous Capital. *European Economic Review*, Vol 43, pp. 253-280.

Baran, Paul & Paul Sweezy. 1966. *Monopoly Capital*. Harmondsworth: Penguin.

Barnes, I. & L. Davidson. 1994. *European Business: Text and Cases*. Oxford, UK: Butterworth-Heinemann.

Baron, David. 2000. *Business and Its Environment* (3rd Edition). Upper Saddle River: Prentice Hall.

Barrell, R. & N. Pain. 1999. Trade restraints and Japanese direct investment flows. *European Economic Review*, 43: 29-45.

Bartlett, Christopher & Sumantra Ghoshal. 1989. *Managing Across Borders: The Transnational Corporation*. Boston, MA: Harvard Business Press.

Baumol, William J. 1982. Contestable markets: an uprising in the theory of industry structure. *American Economic Review*, Vol. 72 (1): 1-15.

Belderbos, René & Leo Sleuwagen. 1996. Japanese Firms and the decision to invest abroad: business groups and regional core networks. *The Review of Economics and Statistic*s, vol.

Belderbos, René. 1997. Antidumping and tariff jumping: Japanese firms' DFI in the European Union and the United States. In: *Weltwirtschaftliches Archiv: Zeitschrift des Instituts für Weltwirtschaft* Kiel, Vol. 133(3), 419-457 (39).

Bergsten, C. Fred. 1997. Open regionalism. Working Paper 97-3, Institute for International Economics.

Bhagwati, Jagdish. 1991. *The World Trading System at Risk*. Princeton: Princeton University Press.

Bhagwati, Jagdish. 1993. Regionalism and multilateralism: an overview. In J. de Melo & A. Panagariya, editors, *New Dimensions in Regional Integration*. Cambridge: Cambridge University Press.

Bilkey, W. & G. Tesar. 1977. The Export Behavior of Smaller-sized Wisconsin Firms. *Journal of International Business Studies*, vol. 8 (spring/summer): 93-98.

Birkinshaw, Julian & Neil Hood. 1997. Determinants of Subsidiary Mandates and Subsidiary Initiative: A Three-Country Study. In: R. Loveridge ed., *Internationalization: Process, Context and Markets*. London: Macmillan.

Björkman, I. & M. Forsgren, eds. 1996. *The Nature of the International Firm*. Copenhagen: Copenhagen Business School Press.

Blank, Stephen & Jeffrey Haar. 1998. Making NAFTA work: US firms and the new North American Business Environment. North-South Center Press, University of Miami.

Blomström, Magnus & Ari Kokko. 1997. Regional integration and foreign direct investment. Working Paper Series in Economics and Finance no. 172, Stockholm School of Economics.

Blomström, Magnus, Ari Kokko & Stephen Globerman. 1998. Regional Economic Integration and Foreign Direct Investment: The North American Experience. NBER Working Paper Series in Economics and Finance no. 269.

Bosworth, Barry, Robert Lawrence & Nora Lustig. 1992. Introduction. In: B. Bosworth, R. Lawrence & N. Lustig, editors, *Assessing the Impact of North American Free Trade*. Washington, DC: The Brookings Institution.

Bowen, Harry, Abraham Hollander & Jean-Marie Viaene. 1998. *Applied International Trade Analysis*. London: MacMillan Press.

Boyer, Robert & Jean-Pierre Durand. 1993. *After Fordism*. London: MacMillan Press, Ltd.

Brainard, Susan. 1997. An empirical assessment of the proximity-concentration trade-off between multinational sales and trade. *American Economic Review*, vol. 87 (4).

Braithwaite, John & Peter Drahos. 2000. *Global Business Regulation*. Cambridge: University Press.

Branch, Ann & Jakob Øhrgaard. 1999. Trapped in the supranational intergovernmental dichotomy: a response to Stone Sweet and Sandholtz. *Journal of European Public Policy*. 6(1): 123-43.

Brodie, Janine. 1997. New state forms, new political spaces. In: R. Boyer & D. Drache, editors, *States Against Markets: the Limits of Globalization*. London: Routledge.

Buckley, Peter & Marc Casson. 1976. The Future of the Multinational Enterprise. London: MacMillan.

Buckley, Peter & Parvez Gauri. 1999. *The Internationalization of the Firm: A Reader*. 2nd ed. London: International Thomson Business Press.

Cable, Vincent & David Henderson. 1994. Overview. In: V. Cable & D. Henderson, editors, *Trade Blocs? The Future of Regional Integration*. London: The Royal Institute of International Affairs.

Cameron, David. 1992. The 1992 initiative: causes and consequences. In: Sbragia, A., editor, *Europolitics: Institutions and Policymaking in the "New" European Community*. Wash, D.C.: The Brookings Institution.

Cameron, Maxwell & Brian Tomlin. 2000. *The Making of NAFTA: How the Deal was Done*. Ithaca: Cornell University Press.

Cameron, Maxwell *et al*. 1992. North American free trade: cooperation and conflict in Canada-Mexico relations. In: F.O. Hampson and C. Maule, editors, *Canada Among Nations 1992-93: A New World Order?* Ottawa: Carlton University Press.

Cantwell, John. 1992. The methodological problems raised by the collection of foreign direct investment data. *Scandinavian International Busienss Review*, 1(1): 86-103.

Cantwell, John. 1993. The reorganization of European industries after integration: selected evidence on the role of multinational enterprise activities. In: J. Dunning & P. Robson, editors, *Multinationals and the European Community*. Oxford: Basil Blackwell.

Cantwell, John. 2000. A survey of theories of international production. In C. Pitelis & R. Sugden, editors, *The Nature of the Transnational Firm*. (2nd Ed.) London: Routledge.

Carr, Edward Hallett. 1951. *The New Society*. London: MacMillan Press.

Casson, Marc & P. McCann. 1999. Globalization, competition and the corporation: the UK experience. In: *The Evolving Corporation: Global Imperatives and National Responses*. The Group of Thirty, Washington, D.C.

Caves, Richard. 1976. Economic models of political choice: Canada's tariff structure. *Canadian Journal of Economics*, vol. 9: 278-300.

Caves, Richard. 1971. International Corporations: The Industrial Economics of Foreign Investment. *Economica*, 38(Feb): 1-27.

Caves, Richard. 1996. *Multinational Enterprise and Economic Analysis*. Cambridge Surveys of Economic Literature, Cambridge University Press.

Centraal Plan Bureau. 1997. The interplay of institutions, trade-offs, performance and trends. In *Challenging Neighbours*, Berlin: Springer Verlag.

Cerny, Philipp. 1999. Globalization, governance and complexity. In: A. Prakash & J. Hart, editors, *Globalization and Governance*. London: Routledge.

Chang, Ha-Joon & Robert Rowthorn. 1995a. Introduction. In: Chang, H. & R. Rowthorn, editors, *The Role of the State in Economic Change*. Oxford, UK: Clarendon Press.

Chang, Ha-Joon & Robert Rowthorn. 1995b. Role of the state in economic change: entrepreneurship and conflict management. In: Chang, H. & R. Rowthorn, editors, *The Role of the State in Economic Change*. Oxford, UK: Clarendon Press.

Chang, Ha-Joon. 1994. *The Political Economy of Industrial Policy*. New York: St Martin's Press.

Clegg, Jeremy & Susan Scott-Green. 1999. FDI capital flows into the EC: the USA and Japan compared. *Journal of Common Market Studies*, 37(4): 597-616.

Clement, Norris, Gustavo del Castillo Vera, James Gerber, William A. Kerr, Alan J. MacFadyen, Stanford Shedd, Eduardo Zepeda and Diana Alarcón. 1999. *North American Economic Integration: Theory and Practice*. Cheltenham, UK: Edward Elgar.

Cohen, Benjamin. 1997. The political economy of currency regions. In: E. Mansfield & H. Milner, editors, *The Political Economy of Regionalism*. New York: Columbia University Press.

Coleman, William & Geoffrey Underhill, editors. 1998. *Regionalism and Global Economic Integration: Europe, Asia and the Americas*. London: Routledge.

Commission of the European Communities (CEC). 1988. The economics of 1992. *European Economy* 35.

Conn, H. & G.Yip. Global Transfer of Critical Capabilities. 1997. *Business Horizons*, 40(1): 22-31.

Connolly, Melissa & Jessica Gunther. 1999. Mercosur: Implications for growth in member countries. *Current Issues in Economics and Finance*, 5(7).

Cowles, Maria G. 1995. Setting the agenda for a new Europe: the ERT and EC 1992. *Journal of Common Market Studies*, 33(4): 501-26.

Cox, Robert. 1989. *Production, Power and World Order*. New York: Columbia University Press.

Cox, Robert. 1994. Global restructuring: making sense of the changing international political economy. In: R. Stubbs & G. Underhill, editors, *Political Economy and the Changing Global Order*. London: MacMillan.

Criekmans, David. 1998. Symbiosis or controversy? Governmental appraisal of lobbying regulation in the EU and USA. PSW paper 1998/3, University of Antwerp.

Crouch, Colin & Wolfgang Streeck. 1997. Introduction: the future of capitalist diversity. In: C. Crouch & W. Streeck, editors, *Political Economy of Modern Capitalism*. London: Sage Publications.

Cyert, Richard & James March. 1963. *A Behavioral Theory of the Firm*. New Jersey: Prentice Hall.

D'Cruz, Joseph & Alan Rugman. 1997. The theory of the flagship firm. *European Management Journal* 15(4): 403-412.

D'Cruz, Joseph, & Alan Rugman. 1992. *New Compacts for Canadian Competitiveness*, Toronto: Kodak Canada.

Daniels, J.D. & Bracker, J. 1989. Profit performance: do foreign operations make a difference? *Management International Review*, 29: 46-56.

Davenport, M. & S. Page. 1991. *Europe: 1992 and the Developing World*. London : ODI.

David, Paul. 1985. Clio and the economics of QWERTY. *American Economic Review Proceedings*, 75: 332-7.

Davies, Stephen, Catherine Matraves, David Petts & Lars-Hendrik Röller. 1999. The corporate structure of UK and German manufacturing firms: changes in response to the SEM. The Anglo-German Foundation for the Study of Industrial Society.

De Bondt, G., P van Els, & A. Stokman. 1997. A macroeconomic multi-country model for the EU. DNB Staff Reports, De Nederlandsche Bank.

De Bono, Edward. 1970. *Lateral Thinking: A Textbook of Creativity*. London: Ward Lock International.

De Melo, Jaime, Arvind Panagariya & Dani Rodrik. 1993. The new regionalism: a country perspective. In: J. de Melo & A. Panagariya, editors, *New Dimensions in Regional Integration*. Cambridge: Cambridge University Press.

Dent, Christopher. 1997. *The New European Economy*. London: Routledge.

Devinney, Timothy & William Hightower. 1991. *European Markets after 1992*. Lexington, MA: Lexington Books.

Dicken, Peter. 1992. *Global Shift*: *Transforming the World Economy*. London: Paul Chapman Publishing.

Dixit, Avanash & Gene Grossman. 1986. Targeted Export Promotion with Several Oligopolistic Industries. *Journal of International Economics*, 21: 233-50.

Douglas, Susan & Yoram Wind. 1987. The Myth of Globalization. *Columbia Journal of World Business*, Winter 1987 (reprinted in De Wit & Meyer, 1998).

Doz, Yves. 1986. Government Policies and Global Industries. In M. Porter, editor, *Competition in Global Industries*. Boston, MA: HBS.

Dudley, Geoffrey & Jeremy Richardson. 1997. Competing Policy Frames in EU Policy Making: The Rise of Free Market Ideas in EU Steel Policy 1985-1996. EIOP vol. 1, 1997.

Dunning, J. & Pearce, R. 1985. *The world's largest industrial enterprises 1962-1983*. New York: St. Martin's Press.

Dunning, John & Alan Rugman. 1985. The Influence of Hymer's Dissertation on the Theory of Foreign Direct Investment. *American Economic Review*, May.

Dunning, John. 1986. *Japanese Participation in British Industry*. London: Croom Helm.

Dunning, John. 1993. *Multinational Enterprises and the Global Economy*. New York: Addison Wesley.

Dunning, John. 1997a. The European Internal Market Programme and Inbound Foreign Direct Investment (Pts I and II). *Journal of Common Market Studies*, 35(2).

Dunning, John. 1997b. *Alliance Capitalism and Global Business*. London: Routledge.

Dunning, John. 1997c. Governments and the Macro-organization of Economic Activity: A Historical and Spatial Perspective. In: J. Dunning, editor, *Governments, Globalization and International Business*. Oxford, UK: Oxford University Press.

Dunning, John. 1998. Location and the Multinational Enterprise: A Neglected Factor? *Journal of International Business*, 29(1): 45-66.

Eaton, C., R. Lipsey & E. Safarian. 1994. The Theory of Multinational Plant Location in an RTA. In: L. Eden, editor, *Multinationals in North America*. Calgary: Univ. of Calgary Press.

Economist. Oct. 28, 2000. Survey Mexico: If not for NAFTA, When?

Eden, Lorraine & Stefanie Lenway. 2001. Introduction to the Symposium Multinationals: the Janus Face of Globalization. *Journal of International Business Studies*, 32, 3: 383-400.

Eden, Lorraine, editor. 1993. *Multinationals in the Global Political Economy*. New York: St. Martin's Press.

Eden, Lorraine, editor. 1994. *Multinationals in North America*. Calgary: University of Calgary Press.

Encarnation, Dennis & Louis Wells, Jr. 1986. Competitive strategies in global industries: a view from host governments. In M. Porter, editor, *Competition in Global Industries*. Boston, MA: HBS.

Ethier, Wilfred. 1998. Regionalism in a Multilateral World. *The Journal of Political Economy*, 106(6): 1214-45.

Ethier, Wilfred. 2001. Punishments and dispute settlement in trade agreements. PENN Working Paper series.

Faux, Jeff & Richard Rothstein. 1991. Fast Track, Fast Shuffle: The Economic Consequences of the Administration's Proposed Trade Agreement with Mexico. Economic Policy Institute Briefing Paper

Feenstra, Robert, Gene Grossman & Douglas Irwin, editors, *The Political Economy of Trade Policy*. London: MIT Press.

Feinberg, Susan & Michael Keane. 2001. U.S.-Canada Trade Liberalization and MNC Production Location, *Review of Economics and Statistics*, vol. 83: 118-132.

Findlay, Ronald. 1993. Discussion to chapter 6, In: J. De Melo & A. Panagariya, editors, *New Dimensions in Regional Integration*. Cambridge: Cambridge University Press.

Flam, Harry. 1992. Product Markets and 1992: Full Integration, Large Gains? *Journal of Economic Perspectives*, vol. 6(4): 7-30.

Fujita, M., P. Krugman & A. Venables. 1999. *The Spatial Economy: Cities, Regions and International Trade*. London: MIT Press.

Gatsios, K. & L. Karp. 1995. Delegation in a General Equilibrium Model of Customs Unions. *European Economic Review*, vol. 39: 391-97.

Gatz, Jürgen. 1997. *The Socio-Economic Impact of NAFTA's FDI Potential for Mexico*. Frankfurt: Peter Lang.

Gawande, Kishore & Wendy Hansen. 1999. Retaliation, bargaining and the pursuit of 'free and fair' trade. *International Organization*, 53(1).

Gestrin, Michael & Alan Rugman. 1994. The strategic response of MNEs to NAFTA. in: Rugman, A., editor, *Foreign Investment and NAFTA*. Columbia: University of South Carolina Press.

Gestrin, Michael V, Rory F. Knight and Alan M. Rugman. 2000. *Templeton Global Performance Index*. Templeton College, Oxford (sponsored by the ESRC).

Ghemawat, Pankaj. 1994. The Short Run versus the Long Run in Cross-sectional Industrial Organization. In: H. Daems & H. Thomas, editors, *Strategic Groups, Strategic Moves and Performance*. Oxford, UK: Pergamon.

Gill, Stephen. 1994. Knowledge, politics and neo-liberal political economy. In: R. Stubbs & G. Underhill, editors, *Political Economy and the Changing Global Order*. London: MacMillan.

Gilpin, Robert. 2001. *Global Political Economy: Understanding the International Economic Order*. Princeton, NJ: Princeton University Press.

Globerman, Steven. 1994. The economics of NAFTA. In: Rugman, A., editor, *Foreign Investment and NAFTA*. Columbia: University of South Carolina Press.

Goerzen, A. & Beamish, P. 2002. Geographic scope and multimational enterprise performance. Paper presented at the Annual Meeting of the Academy of International Business, San Juan Puerto Rico.

Gomes, Leonard & Kannan Ramaswamy. 1999. An empirical examination of the form of the relationship between multinationality and performance. *Journal of International Business Studies* 30: 173-188.

Graham, Edward. 1997. Should there be multilateral rules on FDI? In: J. Dunning, editor, *Governments, Globalization and International Business*. Oxford University Press.

Greenwood, Justin. 1997. *Representing Interests in the European Union*. London: MacMillan Press.

Grossman, Gene & Elhanan Helpman. 1994. Protection for sale. *American Economic Review*, vol. 84(4): 833-51.

Grossman, Gene & Elhanan Helpman. 1995. The politics of free-trade agreements. *American Economic Review*, vol. 85(4): 667-690.

Haas, Ernst. 1958. *The Uniting of Europe*. Stanford: Stanford University Press.

Haggard, Stephen. 1997. The political economy of regionalism in Asia and the Americas. In: E. Mansfield and H. Milner, editors, *The Political Economy of Regionalism*. New York: Columbia University Press.

Hancher, Leigh & Michael Moran. 1989. Introduction. In: L. Hancher & M. Moran, editors, *Captialism, Culture and Regulation*. Oxford: Clarendon Press.

Harzing, Anne-Wil. 2000. An Empirical Ananlysis and Extension of the Bartlett and Ghoshal Typology of Multinational Companies. *Journal of International Business Studies*, 31(1): 101-20.

Helpman, Elhanan & Paul Krugman. 1989. *Trade Policy and Market Structure*. Cambridge, MA: MIT Press.

Helpman, Elhanan. 1985. Multinational Corporations and Trade Structure. *Review of Economic Studies*, vol.. 52: 443-58.

Helpman, Elhanan. 1999. Politics and trade policy. In: R. Baldwin, D. Cohen, A. Sapir and A. Venables, editors, *Market Integration, Regionalism and the Global Economy*. London: Centre for Economic Policy Research.

Hennart, Jean-François. 2000. Transaction Cost Economics. In: C. Pitelis & R. Sugden, editors, *The Nature of the Transnational Firm*. (2nd Ed.) London: Routledge.

Herkströter, C.J. 1996. Breaking European Barriers. *European Business Journal*, vol. 8(1): 56-59.

Hettne, Björn & Frederik Söderbaum. 2000. Theorising the rise of regionness. *New Political Economy*, 5(3): 457-473.

Hirschman, Albert. 1970. *Exit, Voice and Loyalty*. Cambridge, MA: Harvard University Press.

Hirst, Paul & Grahame Thompson. 1999. *Globalization in Question: The International Economy and the Possibilities of Governance*. Cambridge UK: Polity Press.

Hoekman, Bernard & Michel Kostecki. 1995. *The Political Economy of the World Trading System: from GATT to WTO*. Oxford: Oxford University Press.

Hollingsworth, J. Rogers. & Robert Boyer, editors. 1996. *Contemporary Capitalism: The Embeddedness of Institutions*. Cambridge UK: Cambridge University Press.

Hufbauer, Gary & Jeffrey Schott. 1993. *NAFTA: An Assessment*. Washington: Institute for International Economics.

Hufbauer, Gary & Jeffrey Schott. 1994. *Western Hemisphere Economic Integration*. Washington: Institute for International Economics.

Hufbauer, Gary. 1990. *Europe 1992 : An American Perspective*. DC, Brookings.

Hymer, Stephen & Robert Rowthorn. 1970. Multinational Corporations and International Oligopoly: the non-American Challenge. In: C. Kindleberger, editor, *The International Corporation*. Cambridge, MA: MIT Press.

Hymer, Stephen. 1970. The Efficiency (Contradictions) of Multinational Corporations. *American Economic Review*, vol 60, no 2: 441-448.

Hymer, Stephen. 1972. The Internationalization of Capital. *Journal of Economic Issues*, vol 6, no 1: 91-111.

Hymer, Stephen. 1976. *The International Operations of National Firms: A Study of Direct Foreign Investment*. Cambridge, MA: MIT Press (PhD thesis from 1960).

Hymer, Stephen. 1979. The Multinational Corporation and the International Division of Labor. In: R.B. Cohen, N. Felton, M. Nkosi and J. van Liere, editors, *The Multinational Corporation: A Radical Approach.* Cambridge University Press: Cambridge, UK.

Ietto-Gilles, Grazia. 1998. Different conceptual frameworks in the assessment of the degree of internationalization: empirical analysis of various indices for the top 100 TNCs. *Transnational Corporations* 7(1).

IISD-WWF. 2001. *Private Rights, Public Concerns: A Guide to NAFTA's Controversial Chapter on Investor Rights*. Canada.

ILO. 1997. Common Market of the Southern Cone: Mercosur: The impact of economic integration: a case study.

Industry Canada. 2001. Monthly Trade Bulletin, vol 3(10), December. Ottawa.

Jacquemin, Alexis & André Sapir. 1988. International Trade and Integration of the European Community: An Econometric Analysis. *European Economic Review*, 32: 1439-49.

Jessop, Bob. 1999. The Social Embeddedness of the Economy and Its Implications for Economic Governance. In: F. Adaman & P. Devine, eds., *The Socially Embedded Economy*, Montreal: Black Rose Books.

Johanson, J. & J-E. Vahlne. 1977. The Internationalization Process of the Firm – a Model of Knowledge Development and Increasing Foreign Market Commitments. Journal of International Business Studies, 8(1): 23-32.

Johanson, J. & L.-G. Mattsson. 1988. Internationalization in Industrial Systems – a Network Approach. In: N. Hood & J.-E. Vahlne, editors, *Strategies in Global Competition*. New York: Croom Helm.

Johnson, Debra & Colin Turner. 2000. *European Business: Policy Challenges for the New Commercial Environment*. London: Routledge.

Jovanovic, Miroslav. 1992. *International Economic Integration*. London: Routledge.

Jovanovic, Miroslav. 2001. *Geography of Production and Economic Integration*. London: Routledge.

Kemp, Murray & Henry Wan, Jr. 1976. An elementary proposition concerning the formation of Customs Unions. *Journal of International Economics*, vol. 6: 95-97.

Keohane, Robert. 1984. *After Hegemony*. Princeton, NJ: Princeton University Press.

Kindleberger, Charles. 1966. European integration and the international corporation. *Columbia Journal of World Business*, 1, pp. 65-73.

Kindleberger, Charles. 1969. *American Business Abroad: Six Lectures on Direct Investment*. New Haven: Yale University Press.

Knickerbocker, Fredrick. 1973. *Oligopolistic Reaction and Multinational Enterprise*. Boston, MA: Division of Research, Harvard University.

Kobrin, Stephen. 1984. Expropriation as an Attempt to Control Foreign Firms in LDCs: Trends from 1960-79. *International Studies Quarterly*, 28(3): 329-48.

Kobrin, Stephen. 1987. Testing the Bargaining Hypothesis in the Manufacturing Sector in Developing Countries. *International Organization*, vol. 41(4): 609-38.

Kobrin, Stephen. 1991. An Empirical Analysis of the Determinants of Global Integration. *Strategic Management Journal*, 12: 17-31.

Kogut, Bruce & Udo Zander. 1993. Knowledge of the Firm and the Evolutionary Theory of the Multinational Corporation. *Journal of International Business Studies*, Vol. 24(4): 625-46.

Kogut, Bruce. 1984. Normative Observations on the International Value-Added Chain and Strategic Groups. *Journal of International Business Studies*, vol. 15(2): 151-168.

KPMG. 2000. Euro report. KPMG.

Krasner, Stephen. 1978. *Defending the National Interest: Raw Materials, Investments and US Foreign Policy*. Princeton, NJ: Princeton University Press.

Krugman, Paul. 1986. *Strategic Trade Policy and the New International Economics*. Cambridge MA: MIT Press.

Krugman, Paul. 1990. Increasing Returns and Economic Geography. NBER Working Papers 3275, National Bureau of Economic Research.

Krugman, Paul. 1991a. *Geography and Trade*. Cambridge, MA: MIT Press.

Krugman, Paul. 1991b. Is bilateralism bad? In: E. Helpman and A. Razin, editors, *International Trade and Trade Policy*. Cambridge, MA: MIT Press.

Krugman, Paul. 1993. Regionalism vs. multilateralism: analytical notes. In J. de Melo & A. Panagariya, editors, *New Dimensions in Regional Integration*. Cambridge, MA: Cambridge University Press.

Krugman, Paul. 1994. Competitiveness: a dangerous obsession. *Foreign Affairs*. March-April: 28-44.

Kwok, C. & Reeb, D. 2000. Internationalization and firm risk. *Journal of International Business Studies*, vol. 31(4): 611-629.

Laird, Sam. 1997. Mercosur: Objectives and Achievements. WTO Paper presented at Third Annual World Bank Conference on Development in Latin America and the Caribbean, June 29 - July 1, 1997, Montevideo, Uruguay.

Lake, David. 1999. Global governance: a relational contracting approach. In: A. Prakash and J. Hart, editors, *Globalization and Governance*. London: Routledge.

Lall, Sanjaya. 1976. Theories of Direct Foreign Private Investment and Multinational Behaviour. *Economic and Political Weekly*, 11: 31-3.

Lane, Christel. 1992. In: R.Whitley, editor, 1992. *European Business Systems: Firms and Markets in their National Contexts*. London: Sage Publications.

Lazonick, William & M. O'Sullivan, 1996. Organizational, financial and international competition. *Industrial and Corporate Change*, 5 (1) pp. 1-49.

Leamer, Edward. 1995. In search of Stolper-Samuelson effects on US wages. NBER Research Paper no. 5427.

Leaver, Richard. 1994. International political economy and the changing world order: evolution or involution? In: R. Stubbs & G. Underhill, editors, *Political Economy and the Changing Global Order*. London: MacMillan.

Lee, K.C. & Kwok, C. 1988. Multinational corporations vs. domestic corporations: international environmental factors and determinants of capital structure. *Journal of International Business Studies*, vol. 19(2): 195-217.

Levy, Philip. 2000. Assymetric Information and Inference from Free Trade Agreements. Unpublished Working Paper.

Lipsey, R. 2001. Foreign direct investment and the operations of multinational firms: concepts, history and data. *NBER Working Paper Series, no. 8665.* Cambridge, MA: National Bureau of Economic Research. Abbott, Frederick. 1999. The North American Integration Regime and Its Implications for the World Trading System. Jean Monnet Working Paper no. 2/99.

Lipsey, Richard. 1997. Globalization and National Government Policies. In: J. Dunning, editor, *Governments, Globalization and International Business*. Oxford University Press.

Lipsey, Robert. 1990. American Firms Facing Europe: 1992. In: M. Feldstein and Y. Kosai, editors, *US-Japan Economic Forum*. Cambridge, MA: NBER.

Lu, J.W. & Beamish, P. 2000. Internationalization and performance: an examination of the different effects of exporting and FDI. Paper presented at Academy of Management, Toronto.

Lundvall, B. 1993. User-producer Relationships, National Systems of Innovation and Internationalization. In: D. Foray & a. C. Freeman, editors, *Technology and the Wealth of Nations: The Dynamics of Constructed Advantage*. London: Pinter Publishers.

Lung, Yannick & Rob van Tulder. 2004. In Search of a Viable Automobile Space. In: J. Carillo, Y. Lung & Rob van Tulder, editors. *Cars, Carriers of Regionalism*. Palgrave.

Lustig, Nora, Barry Bosworth & Robert Lawrence, editors. 1992. *Assessing the Impact of North American Free Trade*. Washington, D.C.: The Brookings Institution.

Mansfield, Edward & Helen Milner. 2000. The New Wave of Regionalism. *International Organization*, 53(3): 589-627.

Markusen, James R. & Keith E. Maskus. 2001. General-Equilibrium Approaches to the Multinational Firm: A Review of Theory and Evidence. Draft paper presented at NBER, March 2001.

Markusen, James. 1995. The Boundaries of Multinational Enterprises and the Theory of International Trade. *Journal of Economic Perspectives*, 9(2): 169-189.

Markusen, James. 2001. International Trade Theory and International Business. In: A. Rugman & T. Brewer, editors, *The Oxford Handbook of International Business*. Oxford, UK: Oxford University Press.

Martin, Andrew. 1994. Labour and the Keynesian state. In: R. Stubbs & G. Underhill, editors, *Political Economy and the Changing Global Order*. London: MacMillan.

Mattli, Walter. 1999a. Explaining regional outcomes. *Journal of European Public Policy*, 6(1): 1-27.

Mattli, Walter. 1999b. *The Logic of European Integration: Europe and Beyond*. Cambridge, UK: Cambridge University Press.

McCall Smith, James. 2000. The politics of dispute settlement design: explaining legalism in Regional Trade Pacts. *International Organization*, 54(1).

McDonald, Frank & Margaret Potton. 1994. Industrial policy in the EU. In: Frank McDonald & Stephen Dearden, editors, *European Economic Integration*. (2nd ed.). London: Longman.

McDonald, Frank. 1994. Introduction. In: Frank Macdonald & Stephen Dearden, editors, *European Economic Integration*. (2nd ed.). London: Longman.

McGilvray, Fiona. 2000. Bargaining leverage for smaller states: south-south customs unions. Paper presented at the Leitner Conference on Political and Economic Aspects of Regional Integration, Yale University, April 2000.

McGinnis, Michael. 1999. Rent-seeking, Redistribution and Reform in the Governance of Global Markets. In: A. Prakash & J. Hart, editors, *Globalization and Governance*. London: Routledge.

McLaren, John. 2000. Free trade agreements, customs unions and the dynamics of political influence. Paper presented at the Leitner Conference on Political and Economic Aspects of Regional Integration, Yale University, April 2000.

Meade, James. 1956. *The Theory of Customs Unions*. Amsterdam: North Holland.

Melin, Leif. 1992. Internationalization as a Strategy Process. *Strategic Management Journal*, vol. 13: 99-118.

Merriden, Trevor. 1998. How 'single' is the Single Market ? *Management Review*, vol. 87(3): 27-31.

Messerlin, Patrick. 1983. *Bureaucracies and the Political Economy of Protection: Reflections of a Continental European*. World Bank.

Meunier, Sophie. 2000. What single voice? European institutions and EU-US trade negotiations. *International Organization*, 54(1).

Michel, A. & Shaked, I. 1986. Multinational coporations vs. domestic corporations: financial performance and chracteristics. *Journal of International Business Studies*, 13(4): 18-25.

Miller, Danny. 1996. Configurations Revisited. *Strategic Management Journal*, vol. 17(7): 505-512.

Milner, Helen & Peter B. Rosendorff. 1997. Democratic Politics and International Trade Negotiations: Elections and Divided Government as Constraints on Trade Liberalization. *The Journal of Conflict Resolution*, vol. 41(1): 117-146.

Milner, Helen. 1988. *Resisting Protectionism: Global Industries and the Politics of International Trade*. Princeton, NJ: Princeton University Press.

Mintzberg, Henry & J. Waters. 1998. Of strategies, deliberate and emergent. In S. Segal-Horn, editor, *The Strategy Reader*. Oxford: Blackwell Publishers.

Mitrany, David. 1975. *A Functional Theory of Politics*. London: Robertson.

Mokyr, Joel. 1990. *The Lever of Riches: Technological Creativity and Economic Progress*. New York : Oxford University Press.

Molle, Willem & Robert Morsink. 1991. Intra-European direct investment. In B. Bürgenmeier & J. Mucchielli, editors, *Multinationals and Europe 1992: Strategies for the Future*. London: Routledge.

Molle, Willem. 1990. *The Economics of European Integration*. Aldershot: Dartmouth.

Molle, Willem. 2000. *The Economics of European Integration: Theory, Practice, Policy*. (4th ed.) Aldershot, UK: Ashgate.

Moran, Theodore. 1985. *Multinational Corporations: The Political Economy of Foreign Direct Investment*. Lexington: D.C. Heath.

Moravcsik, Andrew. 1998. *The Choice for Europe: Social Purpose and State Power from Messina to Maastricht*. Ithaca, NY: Cornell University Press.

Moravscik, Andrew. 1991. Negotiating the Single European Act: national interests and conventional statecraft in the European Community. *International Organization* 45, Winter 1991: 25-6.

Morrison, Allen and Kendall Roth. 1992. The Regional Solution: an Alternative to Globalization. *Transnational Corporations*, vol. 1(2):

Morrison, Allen. 1990. *Strategies for Global Industries: How US Businesses Compete*. New York: Quorum Books.

Morsink, Robert. 1997. *Corporate Networking and Foreign Direct Investment*. PhD Dissertation, Erasmus University of Rotterdam.

Mucchielli, J. Strategic Advantages for European Firms. In B. Bürgenmeier & J. Mucchielli, editors, *Multinationals and Europe 1992: Strategies for the Future*. London: Routledge.

Muller, Alan & Rob van Tulder. 2002. Macro Intentions, Micro Realities: a Two-level Strategic Approach to the Single European Market. *Multinational Business Review*, vol. X(2): 1-10.

Mundell, Robert. 1961. A Theory of Optimum Currency Areas. *American Economic Review*, 51, November: 509-17.

Nelson and Winter, 1982. *An Evolutionary Theory of Economic Change*. Cambridge, MA: Belknap Press.

Nelson, Richard, editor. 1993. *National Innovation Systems: A Comparative Analysis*. New York: Oxford University Press.

Neto, Raul de Gouvea. 1998. Mercosur: fostering regional economic integration. *Thunderbird International Business Review*, Vol. 40 (6), pp. 585-604

Nobes, C. & Parker, R., editors. 2000. *Comparative international accounting*. 6 ed. London: Prentice Hall.

North, Douglass. 1985. *Institutions, Institutional Change and Economic Performance*. Cambridge, UK: Cambridge University Press.

North, Douglass. 1991. Institutions. *The Journal of Economic Perspectives*, 5(1): 97-112.

OECD. 1996. Regionalism and its Place in the Multilateral Trading System. Paris: OECD.

Ogata, S. 1999. Changes in Japanese corporations. In: *The Evolving Corporation: Global Imperatives and National Responses*. The Group of Thirty, Washington, D.C.

Ohmae, Kenichi. 1990. *The Borderless World: Power and Strategy in the Global Marketplace*. London: Collins.

Orme, William A. 1996. *Understanding NAFTA: Mexico, Free Trade and the New North America.* Austin, TX: University of Texas Press.

Ostry, Sylvia. 1990. *Governments and Corporations in a Shrinking World: Trade and Innovation Policies in the US, Europe and Japan*. New York: Council on Foreign Relations.

Oxley, J. & Schnietz, K. 2001. Globalization derailed? *Journal of International Business Studies*, vol. 32(3): 479-496.

Padoan, Pier C. 1997. Regional agreements as clubs: the European case. In: E. Mansfield and H. Milner, editors, *The Political Economy of Regionalism*. New York: Columbia University Press.

Padoa-Schioppa, Tommaso *et al*. 1987. *Efficiency, Stability, and Equity: a Strategy for the Evolution of the Economic System of the European Community*. Oxford University Press, London.

Panagariya, Arvind & Robert Findlay. 1996. A political economy analysis of free-trade areas and customs unions. In R. Feenstra, G. Grossman & D. Irwin, editors, *The Political Economy of Trade Policy*. London: MIT Press.

Panić, Mića. 1991. The impact of multinationals on national economic policy. In B. Bürgenmeier & J. Mucchielli, editors, *Multinationals and Europe 1992: Strategies for the Future*. London: Routledge.

Panić, Mića. 1995. International economic integration and the changing role of governments. In: Chang, H. and R. Rowthorn, editors, *The Role of the State in Economic Change*. Oxford, UK: Clarendon Press.

Pasquero, Jean. 2000. Regional Market Integration in North America and Corporate Social Management. *Business & Society*, vol. 39(1): 6-23.

Pauwels, Pieter & Paul Matthyssens. 2001. Toward a (More) Dynamic Theory of Internationalization: International Market Withdrawal as Empirical Extreme. In: C. Axinn & P. Matthyssens, editors, *Reassessing the International Firm*. Series: Advances in International Marketing, vol. 11. Amsterdam: Elsevier.

Peck, Jamie & Adam Tickell. 1991. Regulation Theory and the Geographies of Flexible Accumulation: Transitions in Capitalism, Transitions in Theory. SPA Working Paper 12, University of Manchester School of Geography.

Peck, S., W. Ruigrok & C. van der Linde. 2000. Strange Bedfellows? Foreigners on Boards and Top Management Teams. Universität St. Gallen FIM Working Paper.

Pelkmans, Jacques & L. Alan Winters. 1988. *Europe's Domestic Market*. Chatham House Paper 43, London: Royal Institute for International Affairs.

Pelkmans, Jacques. 1997. *European Integration: Methods and Economic Analysis*. The Netherlands: Longman.

Peoples, James & Roger Sugden. 2000. Divide and Rule by Transnational Corporations. In: C. Pitelis and R. Sugden, eds. *The Nature of the Transnational Firm*. 2nd edition, Routledge: London.

Perlmutter, H. & Heenan, D. 1979. *Multinational organization development*. Reading, MA: Addison-Wesley.

Perroux, François. 1950. Economic Space: Theory and Applications. *Quarterly Journal of Economics*, vol. 64: 89-104.

Phelps, Nicholas. 1997. *Multinationals and European Integration: Trade, Investment and Regional Development*. London: Jessica Kingsley.

Piore, Michael J. & Charles F. Sabel. 1984. *The Second Industrial Divide: Possibilities for Prosperity*. USA: Basic Books.

Porter, Michael. 1985. *Competitive Advantage*. New York: Free Press.

Porter, Michael. 1986. Competition in Global Industries: A Conceptual Framework. In M. Porter, ed., *Competition in Global Industries*. Boston, MA: Harvard University Press.

Porter, Michael. 1990. *The Competitive Advantage of Nations*. New York: Free Press.

Porter, Michael. 1998. *Clusters and Competition*. Boston, MA: Harvard Business School Press.

Prahalad, C.K. & Gary Hamel. 1994. Strategy as a Field of Study: Why Search for a new Paradigm? *Strategic Management Journal*, vol. 15, (Summer); Special Issue: Strategy: Search for New Paradigms: 5-16.

Prahalad, C. K. & Gary Hamel. 1990. The Core Competence of the Corporation. *Harvard Business Review*, Vol. 68, No. 5/6.

Prahalad, C.K. & Yves Doz. 1987. *The Multinational Mission: Balancing Local Demands and Global Vision*. New York: Free Press.

Prakash, Aseem & Jeffrey Hart. 1999. Globalization and governance: an introduction. In: A. Prakash and J. Hart, editors, *Globalization and Governance*. London: Routledge.

Proff, Heike. 2002. Business Unit Strategies between Regionalisation and Globalisation. *International Business Review*. Volume 11(2): 231-250.

Prusa, Thomas & Susan Skeath. 2001. The economic and strategic motives for antidumping filings. NBER Working Paper 8424.

Public Citizen. 1997. NAFTA's Broken Promises: Failure to Create US Jobs. http://www.publiccitizen.org/trade/nafta/jobs/articles.cfm?ID=1767 (9/12/2003)

Putnam, Robert D. 1988. Diplomacy and domestic politics: the logic of two-level games. *International Organization* 42(3): 427-60.

Qian, G. & Li, J. 1998. Multinationality, global market diversification, and risk performance for the largest U.S. firms. *Journal of International Management*, 4(2): 149-70.

Ramaswamy, K.,. Galen Kroeck, K. & Renforth, W. 1996. Measuring the degree of internationalization of a firm: a comment. *Journal of International Business Studies*, vol. 27(1): 167-177.

Ramstetter, E.D. 1998. Measuring the size of foreign multinationals in the Asia-Pacific.In Thompson, G., editor, *Economic Dynamism in the Asia-Pacific: The Growth of Integration and Competitiveness*. London & New York: Routledge.

Rein, M. & D. Schön. 1991. Frame-reflective policy discourse. In P. Wagner, C. Hirschon Weiss, B. Wittrock & H. Wollman, editors, *Social Science and Modern States, National Experiences and Theoretical Crossroads*. Cambridge: University Press.

Reynolds, Michael. 1995. Proceedings against Unilever. *International Financial Law Review*, vol. 14(4): 63.

Robson, Peter, editor. 1993. *Transnational Corporations and Regional Economic Integration*. United Nations' Library on Transnational Corporations, vol. 9. London: Routledge.

Rubery, J. 1994. The British production regime: a societal-specific system? *Economy and Society*, 23 (3) pp. 355-73.

Rugman, Alan & Alain Verbeke. 1991. Competitive strategies for non-European firms. In B. Bürgenmeier & J. Mucchielli, editors, *Multinationals and Europe 1992: Strategies for the Future*. London: Routledge.

Rugman, Alan & Alain Verbeke. 1994. Foreign Direct Investment and NAFTA: A conceptual framework. In: Rugman, A., editor, *Foreign Investment and NAFTA*. Columbia: University of South Carolina Press.

Rugman, Alan. 1976. Risk Reduction by International Diversification. *Journal of International Business Studies*, vol. 7(2): 75-80.

Rugman, Alan. 2000. *The End of Globalization*. New York: Random House.

Ruigrok, Winfried & Hardy Wagner. 2003. Internationalization and Performance: An Organizational Learning Perspective. *Management International Review*, vol 43(1): 63-83.

Ruigrok, Winfried & Rob van Tulder. 1995. *The Logic of International Restructuring*. London: Routledge.

Sachwald, Frédérique. 1993. Competitiveness and competition: which theory of the firm? In F. Sachwald, editor, *European integration and competitiveness: Acquisitions and Alliances in Industry*. Aldershot, UK: Edward Elgar Publishing.

Sandholtz, Wayne. 1999. Globalization and the evolution of rules. In: A. Prakash & J. Hart, editors, *Globalization and Governance*. London: Routledge.

Saudagaran, S. & Biddle, G. 1995. Foreign listing location: a study of MNCs and stock exchanges in eight countries. *Journal of International Business Studies*, vol. 26(2): 319-41.

Scharpf, Fritz. 1988. The Joint-Decision Trap: Lessons from German Federalism and European Integration. *Public Administration*, 66(3): 239-278.

Schlie, Erik & George S. Yip, Regional Follows Global: Strategy Mixes in the World Automotive Industry, *European Management Journal*, Vol. 18, No. 4: 343-354.

Schmalensee, Richard. 1989. Studies of Structure and Performance. In: R. Schmalensee & R. Willig, editors, *Handbook of Industrial Organization*, vol. II. Amsterdam: North Holland Press.

Schmitter, Philippe. 1974. Still the Century of Corporatism? *The Review of Politics*, Vol.36, no.1: 93-94.

Schmitter, Philippe. 1996. Imagining the future of the Euro-polity with the help of new concepts. in: Marks *et al*., eds. *Governance in the European Union*. London: Sage Publications, p. 121-150.

Schotter, Andrew. 1981. *The Economic Theory of Social Institutions*. New York: Cambridge University Press.

Schwartz, Herman. 1994. *States versus Markets: History, Geography, and the Development of the International Political Economy*. New York: St. Martin's Press.

Scott, Alan (editor). 1997. *The Limits of Globalization: Cases and Arguments*. London: Routledge.

Scott, Richard. 1995. *Institutions and Organizations*. Thousand Oaks, CA: Sage Publishing.

Shin, S. 1998. *European Integration and Foreign Direct Investment in the EU: The case of the Korean consumer electronics industry*. London: Routledge.

Sietses, Hugo. 2000. The Fragmented Interest Representation of Big Dutch Business in the European Union. Master's Thesis, University of Rotterdam Faculty of Business Studies.

Single Market Review. 1997. *Business Survey 1997*. Luxembourg: CEC.

Sklair, Leslie. 2001. *The Transnationalist Capitalist Class*. Oxford: Blackwell.

Slager, Alfred. 2004. The Internationalization of Banks. PhD Thesis, ERIM (Rotterdam)

Soskice, David. 1991. The institutional Infrastructure for international competitiveness: a comparative analysis of the UK and Germany. In: A.B. Atkinson & R. Brunetta, editors, *Economics for the New Europe*. New York: MacMillan.

Stephan, M. & Pfaffmann, E. 2001. Detecting the pitfalls of data on foreign direct investment: scope and limits of FDI data. *Management International Review*, 41(2): 189-218.

Stone Sweet, Alec & Wayne Sandholtz. 1997. European Integration and Supranational Governance. *Journal of European Public Policy*, vol. 4(3): 297-317.

Stopford, J.M., Dunning, J.H. & Haberich, K.O. 1992. *Directory of multinationals*. 4th ed. Basingstoke: Macmillan.

Stopford, John & Susan Strange. 1991. *Rival States, Rival Firms: Competition for World Market Share*. Cambridge: Cambridge University Press.

Strange, Susan. 1994. Rethinking structural change in the international political economy: states, firms and diplomacy. In: R. Stubbs & G. Underhill, editors, *Political Economy and the Changing Global Order*. London: MacMillan.

Strange, Susan. 1995. The Defective State. *Daedalus*, 124(2), Spring: 55-74.

Strange, Susan. 1997a. An international political economy perspective. In: J. Dunning, editor, *Governments, Globalization and International Business*. Oxford University Press.

Strange, Susan. 1997b. The future of global capitalism; or, will divergence persist forever? In: C. Crouch & W. Streeck, editors, *Political Economy of Modern Capitalism*. London: Sage Publications.

Sugden, Roger. 1991. The Importance of Distributional Considerations. In: C. Pitelis and R. Sugden, eds. *The Nature of the Transnational Firm*. Routledge: London.

Sullivan, Daniel. 1994. Measuring the degree of internationalization of a firm. *Journal of International Business Studies*, vol. 2: 325-342.

Sullivan, Daniel. 1996. Measuring the degree of internationalization of a firm: a reply. *Journal of International Business Studies*, vol. 27(1): 179-192.

Tallman, Stephen & George Yip. 2001. Strategy and the multinational enterprise. In A. Rugman & T. Brewer, editors, *The Oxford Handbook of International Business*. Oxford: Oxford University Press.

Ten Napel, Stephanie. 1998. SADC and the TNCs: Crossing Borders? MA thesis, Faculty of Business Studies, Erasmus Universiteit Rotterdam.

UNCTAD. 1996. Handbook of Economic Integration and Cooperation Groupings of Developing Countries: Vol. 1. Geneva..

UNCTAD. 1997. *World Investment Report*. Geneva.

UNCTAD. 1998. *World Investment Report*. Geneva.

Van den Berghe, Douglas. 2003. *Working Across Borders: Multinational Enterprises and the Internationalization of Employment*. Rotterdam: ERIM.

Van der Pijl, Kees. 1992. *Wereldorde en Machtspolitiek*. Amsterdam: Het Spinhuis.

Van Iterson, A. & R. Olie. 1992. European Business Systems: the Dutch Case. In: R.Whitley, editor, *European Business Systems: Firms and Markets in their National Contexts*. London: Sage Publications.

Van Tulder, Rob & Denis Audet. 2004. The Faster Lane of Regionalism. In: J. Carillo, Y. Lung & Rob van Tulder, editors. *Cars, Carriers of Regionalism*. Palgrave.

Van Tulder, Rob, Douglas van den Berghe & Alan Muller. 2001. *The Scoreboard of Core Companies*. ERIM, Rotterdam.

Van Tulder, Rob. 1999. *Redrawing Organizational Boundaries*. Rotterdam: Sviib/Erasmus University Rotterdam.

Van Tulder, Rob. 1999. Rival Internationalisation Trajectories: The national and regional embeddedness of core firms' internationalisation strategies In: Andrea Eckhardt, Holm-Detlev Koehler, Ludger Pries (editors) *Global Players in lokalen Bindungen*, Berlin: Edition Sigma, pp.53-79

Vernon, Raymond. 1966. International Investment and International Trade in the Product Cycle. *Quarterly Journal of Economics*, pp. 190-207.

Vernon, Raymond. 1971. *Sovereignty at Bay: The Multinational Spread of US Enterprises*. New York: Basic Books, Inc.

Vernon, Raymond. 1993. Sovereignty at Bay: 20 Years After. In L. Eden, editor, *Multinationals In the Global Political Economy*. London: MacMillan Press.

Vernon, Raymond. 1994. Multinationals and governments: key actors in the NAFTA. In: L. Eden, editor, *Multinationals in North America*. Calgary: Univ. of Calgary Press.

Vernon, Raymond. 1998. *In the Hurricane's Eye*. Cambridge, MA: Harvard University Press.

Viner, Jacob. 1950. *The Customs Union Issue*. New York: Carnegie Endowment for International Peace.

Waltz, Kenneth. 1979. *Theory of International Politics*. Reading, MA: Addison-Wesley.

Wartick, Steven & Donna Wood. 1998. *International Business & Society*. Oxford: Blackwell Publishers.

Waverman, L.. 1991. Strategic Trade Policy and 1992. In B. Bürgenmeier & J. Mucchielli, editors, *Multinationals and Europe 1992: Strategies for the Future*. London: Routledge.

Weintraub, Sidney. 1992. NAFTA: A US Perspective. In: S. Globerman & M. Walker, editors, *NAFTA: A Trinational Analysis*. Vancouver, BC: The Fraser Institute.

Weintraub, Sidney. 1993. Modeling the Industrial Effects of NAFTA. In: N. Lustig, B. Bosworth & R. Lawrence, editors, *Assessing the Impact of North American Free Trade*. Washington, DC: The Brookings Institution.

Weisfelder, Christine. 2001. Internationalization and the Multinational Enterprise: Development of a Research Tradition. In: C. Axinn & P. Matthyssens, editors, *Reassessing the International Firm*. Series: Advances in International Marketing, vol. 11. Amsterdam: Elsevier.

Whitley, Richard & Peer Hull Kristensen, editors. 1996. *The Changing European Firm: Limits to Convergence*. London: Routledge.

Whitley, Richard & Peer Hull Kristensen, editors. 1997. *Governance at Work: the Social Regulation of Economic Relations*. Oxford: Oxford University Press.

Whitley, Richard, editor. 1992. *European Business Systems: Firms and Markets in their National Contexts*. London: Sage Publications.

Whitley, Richard. 1994. Dominant forms of economic organization in market economies. In: *Organization Studies*, vol. 15(2) pp. 153-182.

Whitley, Richard. 1999. *Divergent Capitalism. The Social Structuring and Change of Business Systems*. Oxford: Oxford University Press.

Wilkinson, F. 1983. Productive systems. *Cambridge Journal of Economics*, 7 (3-4) pp. 413-30.

Willenbockel, Dirk. 1994. *Applied General Equilibrium Modelling: Imperfect Competition and European Integration*. Chichester, UK: Wiley.

Winters, Alan L. 1993. The European Union: a case of successful integration? In: J. de Melo & A. Panagariya, editors, *New Dimensions in Regional Integration*. Cambridge: Cambridge University Press.

Winters, Alan L. 1999. Regionalism versus Multilateralism. In: R. Baldwin, D. Cohen, A. Sapir and A. Venables, editors, *Market Integration, Regionalism and the Global Economy*. London: Centre for Economic Policy Research.

Winters, L. Alan & Anthony Venables. 1991. *European Integration: Trade and Industry*. London: Cambridge University Press.

Winters, L. Alan. 1992. *Trade Flows and Trade Policy after 1992*. London: Cambridge University Press.

WTO. 1995. *Regionalism and the World Trading System*. Switzerland: Geneva.

WTO. 2000. *Mapping of Regional Trade Agreements*. WT/REG/W/41, 11 October 2000.

Yamin, Mohammad. 1991. Hymer's Contribution to TNC Theory. In: C. Pitelis and R. Sugden, eds. *The Nature of the Transnational Firm*. Routledge: London.

Yannopoulos, G. 1992. Multinational Corporations and the Single Market. In: J. Cantwell, editor. *Multinational Investment in Modern Europe: Strategic Interaction in the Integrated Community*. Aldershot UK: Edward Elgar.

Yetati, Eduardo & Frederico Sturzenegger. 1999. The Euro and Latin America III: Is EMU a Blueprint for Mercosur? mimeo, Universidad Torcutato di Tella Business School.

Yeung, M. & N. Perdikis. 1999. *Regional Trading Blocs in the Global Economy: The EU and ASEAN*. Cheltenam, UK: Elgar Publishing.

Yoshida, Masami, Ichiro Akimune, Masayuki Nohara and Kimitoshi Sato. 1994. Regional Economic Integration in East Asia: Special Features and Policy Implications. In: V. Cable & D. Henderson, editors, *Trade Blocs? The Future of Regional Integration*. London: The Royal Institute of International Affairs.

Young, Alisdair. 2001. Extending European Cooperation: the European Union and the 'New' International Trade Agenda. Workshop Paper, ECPR Joint Sessions, April.

Young, Stephen. & J. Hamill, editors. 1992. *Europe and the Multinationals*. Aldershot, UK: Edward Elgar.

Zou, S. & T. Cavusgil. 1996. Global Strategy: A Review and an Integrated Conceptual Framework. *European Journal of Marketing*, 30(1): 52-69.

Zylbersztajn, D. & M. S. Jank. 1998. Agribusiness in Mercosur: Building New Institutional Apparatus. *Agribusiness*, 14 (4).

SAMENVATTING (IN DUTCH)

Het fenomeen 'globalisering', door velen in verband gebracht met liberalisering, vrijhandel en sterk toegenomen internationale investeringen, is een van de meest besproken – maar ook een van de slechts begrepen – begrippen van de jaren negentig. Er wordt vaak gedacht aan multinationale ondernemingen, die een steeds grotere reikwijdte zouden hebben en steeds beter in staat zouden zijn hun productie over de hele wereld te kunnen verplaatsen. Nationale overheden zien hierin een dreiging voor hun eigen beleid en proberen via internationale- of supranationale afspraken vat te krijgen op de mondiale economie en de positie van hun eigen economie en ondernemingen daarin zeker te stellen. Paradoxaal wellicht, is een van de meest voorkomende vormen van supranationale samenwerking daarbij marktintegratie op regionale schaal.

De sterke groei in de jaren negentig van het aantal regionale integratieovereenkomsten ('Regional Integration Agreements', of RIAs), heeft ervoor gezorgd dat 'regionalisering' weer hoog op de agenda staat als onderwerp van onderzoek en theorievorming. De 'eerste golf' van regionalisering vond plaats in de jaren zestig en zeventig, vooral tussen ontwikkelingslanden en werd veelal beschouwd als een mislukking. De huidige 'tweede golf' verschilt van de eerste golf in meerdere opzichten en is veelzijdiger, waardoor het als fenomeen op zich al veel complexer is. De betekenis van integratie kan daarbij op verschillende manieren worden geanalyseerd en opgevat; soms positief, soms negatief en soms gewoon als 'niets nieuws onder de zon'. Zijn RIAs duurzaam – here to stay – of zijn ze de uiting van politiek realisme, improvisatietalent en korte-termijn denken? Zijn ze een stap naar globalisering, of juist barrière daartoe? De verwarring is groot omdat de huidige netwerkeconomie geen makkelijke eenduidige antwoorden toelaat, maar vooral ook – en dat is de insteek van deze studie – omdat de complexiteit van het probleem in zowel wetenschap, bedrijfsstrategie als beleid onderschat wordt.

Regionale integratie kan worden gezien als een proces van internationale herstructurering, waarbij nieuwe instituties vorm krijgen door het gedrag van – en interacties tussen – verschillende belanghebbende actoren. Ondernemingen en overheden zijn daarbij de belangrijkste actoren. Het begrijpen van internationale herstructureringsprocessen en hun uitkomst is daarmee onderhevig aan de spanning tussen verschillende analyseniveaus. Nationale overheden percipiëren 'de' wereld namelijk op macroniveau, omdat dit noodzakelijk is voor het formuleren van beleid op het niveau van samenlevingen en gehele economieën. Ondernemingen daarentegen opereren vanuit een micro-perspectief, vooral rekening houdend met hun eigen belangen en die van hun partners in de waardeketen en de concurrenten. Strategische belangen van overheden en ondernemingen kunnen sterk verschillen, terwijl ze wel verweven zijn door de tijd en ruimte. In de praktijk blijkt vaak dat overheden en ondernemingen dezelfde strategische intenties noch dezelfde perceptie van de werkelijkheid delen.

De interactie tussen percepties en intenties bepaalt echter in sterke mate het succes van de uitkomst van de gekozen strategieën. Als actoren in een dynamisch proces hebben overheden en ondernemingen percepties van elkaars strategische intenties en strategische werkelijkheid. Hierdoor kunnen deze actoren elkaar verkeerd inschatten en uitgaan van foutieve assumpties. Overheden kunnen bijvoorbeeld beleid aannemen met de verwachting dat ondernemingen op een bepaalde manier zullen reageren, terwijl ondernemingen daar heel anders over denken – of daar nog geen specifieke gedachten over hebben. Dit kan

gevolgen hebben voor de uitkomsten van herstructureringsprocessen, vooral in termen van de ruimtelijke configuratie van economische activiteit en de daarmee gepaard gaande verdeling van economische- en maatschappelijke meerwaarde. Machtsverhoudingen spelen bij dergelijke verdelingsvraagstukken altijd een rol. Een relatief kleine groep 'kernondernemingen', meestal grote bedrijven met sleutelposities in de economie, politieke visie en toegang tot politieke actoren, geven bepaalde politieke trajecten niet alleen legitimiteit, maar bepalen ook in sterke mate hun effectiviteit van implementatie. Internationale politieke- en economische herstructurering is in de praktijk vaak een spel met een relatief beperkt aantal spelers, gekenmerkt door oligopolistische 'concurrentie' op zowel macro- als microniveau.

De meest gangbare wetenschappelijke benaderingen van regionale integratie vertonen vanuit dit perspectief tekortkomingen in zowel descriptief, prescriptief als voorspellend opzicht. Ten eerste wordt integratie vaak als een eenvoudige zaak gezien. In menig model worden RIAs zelfs als exogeen gezien (niet beïnvloedbaar door de spelers), of als een rationele beslissing gericht op een maximalisering van welvaart. Integratie kan echter ook als wenselijk worden gezien in een politiek-realistische benadering waarin regionale integratie belangrijk is om macht te genereren in de concurrentie tussen regionale blokken. Regionale integratie is dan zeker geen 'tweederangs' aanpak van mondiale vrijhandel, maar een doel op zich. Ten tweede wordt zelden rekening gehouden met de daadwerkelijke strategieën van ondernemingen, noch als actoren betrokken bij de totstandkoming van de overeenkomst, noch als strategisch diverse spelers in een herstructureringsspel met mogelijk 'sub-optimale' uitkomsten. Veel Regionale Integratie Overeenkomsten zijn gebaseerd op sterk geabstraheerde macro-economische modellen van de werkelijkheid, waarbij het ondernemingsstrategisch niveau er tamelijk bekaaid van af komt, er nauwelijks sprake is van meerdere strategieën en ondernemers een hoge vorm van rationaliteit wordt toegedicht die in de bedrijfskundige literatuur zelden wordt aangetroffen.

Op een paar studies na, is onderzoek dat macro en microniveaus aan elkaar probeert te koppelen schaars gebleven. Theorievorming op het gebied van internationalisering richt zich bijna uitsluitend op de kenmerken van ondernemingen en gaat zelden in op de discussie over 'locatie' op zich. Empirisch onderzoek komt vaak niet verder dan geaggregeerde data en verwachtingen, vooral op basis van stromen van directe buitenlandse investeringen (DBI). DBI is misschien een indicator van ondernemingsactiviteit, maar zegt weinig over de vraag *wie* internationaliseert en *waarom*. Andere studies gaan wel in op de motieven van ondernemingen maar behandelen de argumenten achter regionale integratie vaak oppervlakkig. Kleinschalig onderzoek gericht op een bepaalde regio en een bepaalde sector (zoals de automobiel- of de textielindustrie) komt wel voor, maar plaatst de analyse zelden in een breder (politiek-economisch) raamwerk. Deze studie hoort bij een nieuwe onderzoeksagenda die meer aandacht schenkt aan de geografische spreiding van economische activiteit binnen de context van ondernemingsstrategieën.

In de onderzoeksvraag van deze studie is regionale integratie nadrukkelijk benaderd als een institutionele en economische uitkomst gerealiseerd door het strategisch gedrag van ondernemingen en overheden. De studie gaat specifiek in op de misvattingen die kunnen bestaan tussen macro- en micro en hoe gerealiseerde uitkomsten kunnen verschillen van de verwachte uitkomsten. De overkoepelende vraag luidt als volgt:

In hoeverre organiseren ondernemingen naar aanleiding van de tweede golf van regionale integratie de geografische spreiding van hun activiteiten op de manier die overheden verwachten, en welke conclusies kunnen we hieruit trekken voor de betekenis en duurzaamheid van regionale integratie als strategie voor internationale herstructurering?

Deze vraag is onderzocht door de achtergronden van verschillende RIAs te onderzoeken. De gemeenschappelijke markt, of 'Single European Market' (SEM) in Europa en de vrijhandelsovereenkomst in Noord Amerika, het North American Free Trade Agreement (NAFTA) zijn van alle RIAs veruit de twee belangrijkste. Achterliggende motieven van overheden voor regionale integratie zijn geanalyseerd naar de verwachte uitkomsten in termen van regionale 'openheid'. Openheid heeft betrekking tot de effecten van integratie op verschuiving in productie 1) *binnen* de regio door lokale (regionale) ondernemingen ('inside-in'); 2) *naar* de regio door ondernemingen van buiten de regio ('outside-in'); 3) naar *buiten* toe door regionale ondernemingen ('inside-out'); en als laatste 4) verschuivingen tussen *niet*-lidstaten door spelers van buiten de regio ('outside-out').
'Openheid' is ten eerste bekeken aan de hand van handels- en investeringsdata om te kijken of macro-data de macro-verwachtingen onderbouwen. Uit de analyse van internationale handelsdata wordt bijvoorbeeld duidelijk dat Europa naar binnen toe gekeerd is omdat intra-regionale handel veel omvangrijker is dan handel met partners buiten de regio. De NAFTA-landen daarentegen waren van oudsher naar buiten gericht, maar zijn dat sinds 1997 niet meer. De relatieve geslotenheid van 's werelds twee belangrijkste regio's staat in schril contrast met de oriëntatie van andere regio's zoals de *Mercado Común del Sur* (Mercosur), de *Association of South East Asian Nations* (ASEAN) en de *Southern African Development Community* (SADC), die allemaal erg naar buiten toe gericht waren en dat onder de tweede regionaliseringsgolf steeds meer zijn geworden.
Tegelijkertijd laten internationale investeringsstromen zien dat Europese economieën nauwelijks een externe oriëntatie hebben omdat ze net zoveel in elkaar investeren als in de hele rest van de wereld. Hoewel door Noord Amerikaanse actoren wel meer dan drie keer zoveel buiten de eigen regio wordt geïnvesteerd als daarbinnen, moet dit vooral gezien worden in het licht van de dominantie van de VS als enige betekenisvolle investeerder binnen de regio en de kleine omvang van de Mexicaans en Canadese economieën in verhouding tot de rest van de wereld. Investeringen vanuit de VS naar de twee andere lidstaten groeiden veel sneller dan hun bruto binnenlands product (BBP), hetgeen tevens de conclusie rechtvaardigt dat regionale integratie aanleiding tot een relatief naar-binnen gerichte oriëntatie heeft gegeven.
Uit deze macro-ontwikkelingen blijft het echter nog steeds moeilijk om ondernemingstrategieëen te destilleren. Deze studie heeft deze kloof proberen te overbruggen door de gerealiseerde internationaliseringstrategieëen van de 122 grootste industriële ondernemingen uit Europa en Noord Amerika over de periode 1990-2001 in kaart te brengen. Deze kernondernemingen zijn bij uitstek de actoren die het beste in staat zijn op de institutionele veranderingen in te springen en hebben ook een voorbeeldfunctie voor andere bedrijven. Daarbij hebben deze ondernemingen een belangrijke rol gespeeld bij integratie in Europa en Noord Amerika door via lobbypraktijken en een sterke aanwezigheid in de media sterk aan te dringen op regionale integratie.
Het onderzoek laat zien dat regionalisering het multilateraal systeem heeft ingehaald als de belangrijkste strategie voor internationale herstructurering. Daarbinnen zijn de SEM en de

NAFTA de bi-regionale kern geworden van de mondiale economie. Voor kernondernemingen uit deze twee regio's is regionalisering het meest effectieve institutionele kader gebleken waarbinnen zij hun kernposities kunnen verdedigen en verstevigen. Deze studie differentieert sterk tussen de verschillende strategieën die ondernemingen aan (kunnen) nemen binnen een scala van oriëntaties: op het thuisland gericht ('domestic'), op de thuisregio gericht ('regionaal'), verspreid over twee regio's ('bi-regionaal', hetgeen in de praktijk altijd Europa en Noord Amerika bleek te zijn) of over (meer dan) drie regio's verspreid ('mondiaal'). In tegenstelling tot de 'ideologie' van globalisering/mondialisering blijken de strategieën van kernondernemingen en de migraties hierin over de jaren negentig – in anticipatie en als gevolg van regionalisering – zich voornamelijk in de thuisregio afgespeeld hebben. Regionaal georiënteerde ondernemingen bijvoorbeeld, in beide regio's de grootste cluster, vormden in 2001 nog steeds de grootste groep. De golf van fusies en acquisities in de tweede helft van de jaren negentig betrof ook voornamelijk kernondernemingen met een regionale oriëntatie, die relatief gesproken drie keer zoveel kans maakten overgenomen te worden als ondernemingen met een andere oriëntatie.

Het beeld is allerminst statisch – er is veel migratie tussen 'oriëntaties' geweest en de gemiddelde graad van internationalisering (ook extra-regionaal) is toegenomen. Veel ondernemingen die in 1990 nog voornamelijk op het thuisland waren gericht hebben sterk binnen de regio geïnternationaliseerd, terwijl veel ondernemingen die voorheen al regionaal georiënteerd waren, dat in toenemende mate zijn geworden. Maar andere regionale spelers, vooral in Europa, hebben integratie in de thuisregio juist gebruikt als 'springplank' om extra-regionale posities op te bouwen. Het relatief kleine aantal mondiale ondernemingen – maar negen van de 122 ondernemingen in de studie – heeft deze positie weten te behouden. Maar deze groep is in de loop van de jaren negentig niet groter geworden.

Er heeft teglijkertijd echter ook *de*-internationalisering plaatsgevonden. De Noord Amerikaanse ondernemingen die onder de vorming van NAFTA hun strategieën het meest hebben aangepast, zoals de grote Amerikaanse autofabrikanten, hebben zich voor een deel teruggetrokken in hun thuisregio. Veel bi-regionale ondernemingen (zowel Europees als Noord-Amerikaans) hadden veel moeite met de parallele 'zuigkracht' van de twee regio's en hebben zich gedeeltelijk uit de tweede regio teruggetrokken, of activiteiten buiten de twee regio's afgestoten om zich op hun bi-regionale kern te concentreren. Zo is er een 'kloof' ontstaan tussen regionaal- en mondiaal georiënteerde strategieën. Maar ook bij sommige 'global' ondernemingen, die weliswaar mondiaal zijn gebleven, heeft de-internationalisering plaatsgevonden. Bij de meeste ondernemingen is ook de rol van de tweede regio (Europa voor Noord Amerikaanse kernondernemingen en vice versa) relatief en soms ook absoluut verminderd; groei is voornamelijk gezocht *binnen* de eigen regio en / of *buiten* de tweede regio.

Het resultaat van al deze ontwikkelingen is in ieder geval een toenemende polarisering tussen Noord Amerikaanse en Europese kernondernemingen en dus ook een sterk 'diadiserende' wereldeconomie met een bi-regionale kern en voor elke regio een eigen 'periferie'. Hieruit blijkt dat regionalisering beter lijkt te stroken met de belangen van kernondernemingen dan met die van (sommige) overheden. De neiging naar verdere regionalisering en consolidatie van bestaande regio's (de 'derde golf van regionalisering' middels uitbreiding van de EU en de onderhandelingen voor een vrijhandelsakkoord voor het gehele Amerikaanse halfrond, de FTAA) heeft ook veel steun ondervonden bij

kernondernemingen die graag hun regionale productienetwerken willen uitbreiden. Maar de aarzeling bijvoorbeeld onder Europese overheden om arbeiders uit de nieuwe lidstaten toe te laten wijst er ook op dat ook bij deze derde golf van regionalisering de visies van ondernemingen en overheden nog steeds uiteen kunnen lopen.

BIOGRAPHY

Alan Muller is currently a researcher at the Erasmus University Rotterdam and research director of the SCOPE Expert Center, through which he has been involved in research projects for *inter alia* the Dutch Directorate for Development Cooperation and ICCO. His research focuses on company strategies under regional integration, business-government interaction, development issues, bargaining dynamics and international political economy. He has published in the Multinational Business Review and presented numerous papers at academic conferences such as the AIB and AOM annual meetings. At the annual meeting of the European International Business Academy in 2001, he was awarded the 'Most Challenging Thesis Proposal Award' along with a cash prize in recognition of his ground-breaking approach to his PhD research topic.

Alan Muller was born in the United States and attended high school at Garfield High School in Seattle, Washington. He received his undergraduate degree *cum laude* from the University of Washington's Department of History in 1993, and participated in an exchange program with the University of Aberdeen, Scotland in 1991-92. Following graduation Alan went to Vienna, Austria as a Fulbright Teaching Assistant, where he assisted English teachers at several high schools while continuing his study in Modern European History. In 1995 he entered a Master's degree program in International Relations at the University of Amsterdam, graduating *cum laude* in 1998 with a thesis on 'Stolper-Samuelson and the Effects of Trade on Mexican Wages'.

Previous jobs include work as a strategy consultant for Fource Consultancy Group in high-tech industries. Alan has also worked as desk editor for the ANP (Dutch national press agency) and taught English freelance at language institutes in Vienna and Amsterdam. He lives in Haarlem, the Netherlands, with his wife Sofie and two sons, Carter and Finn.

ERASMUS RESEARCH INSTITUTE OF MANAGEMENT (ERIM)

ERIM PH.D. SERIES
RESEARCH IN MANAGEMENT

ERIM Electronic Series Portal: http://hdl.handle.net/1765/1

Berghe, D.A.F., *Working Across Borders: Multinational Enterprises and the Internationalization of Employment.* (co) Promotor(s): Prof.dr. R.J.M. van Tulder & Prof.dr. E.J.J. Schenk, EPS-2003-029-ORG, ISBN 90-5892-05-34, http://hdl.handle.net/1041

Bijman, W.J.J., *Essays on Agricultural Co-operatives; Governance Structure in Fruit and Vegetable Chains*, (co-) Promotor(s): Prof.dr. G.W.J. Hendrikse, EPS-2002-015-ORG, ISBN: 90-5892-024-0, http://hdl.handle.net/1765/867

Brito, M.P. de, *Managing Reverse Logistics or Reversing Logistics Management? (*co-) Promotor(s): Prof.dr.ir. R. Dekker & Prof.dr. M. B. M. de Koster, EPS-2004-035-LIS, ISBN: 90-5892-058-5, http://hdl.handle.net/1765/1132

Campbell, R.A.J., *Rethinking Risk in International Financial Markets*, (co-) Promotor(s): Prof.dr. C.G. Koedijk, EPS-2001-005-F&A, ISBN: 90-5892-008-9, http://hdl.handle.net/1765/306

Chen, Y., *Labour flexibility in China's companies: an empirical study*, (co-) Promotor(s): Prof.dr. A. Buitendam & Prof.dr. B. Krug, EPS-2001-006-ORG, ISBN: 90-5892-012-7, http://hdl.handle.net/1765/307

Delporte-Vermeiren, D.J.E., *Improving the flexibility and profitability of ICT-enabled business networks: an assessment method and tool*, (co-) Promotor(s): Prof.mr.dr. P.H.M. Vervest & Prof.dr.ir. H.W.G.M. van Heck, EPS-2003-021-LIS, ISBN: 90-5892-040-2, http://hdl.handle.net/1765/359

Dijksterhuis, M., *Organizational dynamics of cognition and action in the changing Dutch and U.S. banking industries*, (co-) Promotor(s): Prof.dr. F.A.J. van den Bosch & Prof.dr. H.W. Volberda, EPS-2003-026-STR, ISBN: 90-5892-048-8, http://hdl.handle.net/1037

Fenema, P.C. van, *Coordination and Control of Globally Distributed Software Projects*, (co-) Promotor(s): Prof.dr. K. Kumar, EPS-2002-019-LIS, ISBN: 90-5892-030-5, http://hdl.handle.net/1765/360

Fleischmann, M., *Quantitative Models for Reverse Logistics*, (co-) Promoter(es): Prof.dr.ir. J.A.E.E. van Nunen & Prof.dr.ir. R. Dekker, EPS-2000-002-LIS, ISBN: 3540 417 117, http://hdl.handle.net/1044

Flier, B., *Strategic Renewal of European Financial Incumbents; Coevolution of Environmental Selection, Institutional Effects, and Managerial Intentionality*, (co Promotor(s): Prof.dr.ing. F.A.J. van den Bosch & Prof.dr. H.W. Volberda, EPS-2003-033-STR, ISBN: 90–5892–055–0, http://hdl.handle.net/1765/1071

Fok, D., *Advanced Econometric Marketing Models*, (co-) Promotor(s): Prof.dr. P.H.B.F. Franses, EPS-2003-027-MKT, ISBN: 90-5892-049-6, http://hdl.handle.net/1035

Ganzaroli , A., *Creating Trust between Local and Global Systems*, (co-) Promotor(s): Prof.dr. K. Kumar & Prof.dr. R.M. Lee, EPS-2002-018-LIS, ISBN: 90-5892-031-3, http://hdl.handle.net/1765/361

Gilsing, V.A., *Exploration, Exploitation and Co-evolution in Innovation Networks*. (co) Promotor(s): Prof.dr. B. Nooteboom & Prof.dr. J.P.M. Groenewegen, EPS-2003-032-ORG, ISBN 90-5892-05-42, http://hdl.handle.net/1040

Graaf, G. de, *Tractable Morality. Customer discourses of bankers, veterinarians and charity workers.* (co-) Promotor(s): Prof.dr. F. Leijnse & Prof.dr. T. van Willigenburg. EPS-2003-031-ORG, ISBN 90–5892–051–8, http://hdl.handle.net/1038

Heugens, P.M.A.R., *Strategic Issues Management: Implications for Corporate Performance*, (co-) Promotor(s): Prof.dr.ing. F.A.J. van den Bosch & Prof.dr. C.B.M. van Riel, EPS-2001-007-STR, ISBN: 90-5892-009-7, http://hdl.handle.net/1765/358

Hooghiemstra, R., *The Construction of Reality*, (co-) Promotor(s): Prof.dr. L.G. van der Tas RA & Prof.dr. A.Th.H. Pruyn, EPS-2003-025-F&A, ISBN: 90-5892-047-X, http://hdl.handle.net/1765/871

Jong, C. de, *Dealing with Derivatives: Studies on the role, informational content and pricing of financial derivatives*, (co-) Promotor(s): Prof.dr. C.G. Koedijk, ISBN: 90-5892-043-7, http://hdl.handle.net/1043

Koppius, O.R., *Information Architecture and Electronic Market Performance*, (co-) Promotor(s): Prof.dr. P.H.M. Vervest & Prof.dr.ir. H.W.G.M. van Heck, EPS-2002-013-LIS, ISBN: 90-5892-023-2, http://hdl.handle.net/1765/921

Langen, P.W. de, *The Performance of Seaport Clusters; A Framework to Analyze Cluster Performance and an Application to the Seaport Clusters of Durban, Rotterdam and the Lower Mississippi*, (co-) Promotor(es): Prof.dr. B. Nooteboom & Prof.drs. H.W.H. Welters, EPS-2004-034-LIS, ISBN: 90-5892-056-9, http://hdl.handle.net/1765/1133

Loef, J., *Incongruity between Ads and Consumer Expectations of Advertising*, (co-) Promotor(s): Prof.dr. W.F. van Raaij & prof. dr. G. Antonides, EPS-2002-017-MKT, ISBN: 90-5892-028-3, http://hdl.handle.net/1765/869

Meer, J.R. van der, *Operational Control of Internal Transport*, (co-) Promotor(s): Prof.dr. M.B.M. de Koster & Prof.dr.ir. R. Dekker, EPS-2000-001-LIS, ISBN:90-5892-004-6, http://hdl.handle.net/1765/859

Miltenburg, P.R., *Effects of modular sourcing on manufacturing flexibility in the automotive industry. A study among German OEMs.* (co) Promotor(s): Prof.dr. J. Paauwe & Prof.dr. H.R. Commandeur, EPS-2003-030-ORG, ISBN 90-5892-052-6, http://hdl.handle.net/1039

Mol, M.M., *Outsourcing, Supplier-relations and Internationalisation: Global Source Strategy as a chinese puzzle*, (co-) Promotor(s): Prof.dr. R.J.M. van Tulder, EPS-2001-010-ORG, ISBN: 90-5892- 014-3, http://hdl.handle.net/1765/355

Oosterhout, J. van., *The Quest for Legitimacy; On Authority and Responsibility in Governance*, (co-) Promotor(s): Prof.dr. T. van Willigenburg & Prof.mr. H.R. van Gunsteren, EPS-2002-012-ORG, ISBN: 90-5892-022-4, http://hdl.handle.net/1765/362

Peeters, L.W.P., *Cyclic Railway Timetable Optimization*, (co-) Promotor(s): Prof. Dr. L.G. Kroon & Prof.dr.ir. J.A.E.E. van Nunen, EPS-2003-022-LIS, ISBN: 90-5892-042-9, http://hdl.handle.net/1765/429

Puvanasvari Ratnasingam , P., *Interorganizational Trust in Business to Business E-Commerce*, (co-) Promotor(s): Prof.dr. K. Kumar & Prof.dr. H.G. van Dissel, EPS-2001-009-LIS, ISBN: 90-5892-017-8, http://hdl.handle.net/1765/356

Romero Morales, D., *Optimization Problems in Supply Chain Management*, (co-) Promotor(s): Prof.dr.ir. J.A.E.E. van Nunen & Dr. H.E. Romeijn, EPS-2000-003-LIS, ISBN: 90-9014078-6, http://hdl.handle.net/1765/865

Roodbergen , K.J., *Layout and Routing Methods for Warehouses*, (co-) Promotor(s): Prof.dr. M.B.M. de Koster & Prof.dr.ir. J.A.E.E. van Nunen, EPS-2001-004-LIS, ISBN: 90-5892-005-4, http://hdl.handle.net/1765/861

Speklé, R.F., *Beyond Generics; A closer look at Hybrid and Hierarchical Governance*, (co-) Promotor(s): Prof.dr. M.A. van Hoepen RA, EPS-2001-008-F&A, ISBN: 90-5892-011-9, http://hdl.handle.net/1765/357

Teunter, L.H., *Analysis of Sales Promotion Effects on Household Purchase Behavior*, (co-) Promotor(s):Prof.dr. ir. B. Wierenga & Prof.dr. T. Kloek, EPS-2002-015-ORG, ISBN: 90-5892-029-1, http://hdl.handle.net/1765/868

Vis, I.F.A., *Planning and Control Concepts for Material Handling Systems*, (co-) Promotor(s): Prof.dr. M.B.M. de Koster & Prof. dr. ir. R. Dekker, EPS-2002-014-LIS, ISBN: 90-5892-021-6, http://hdl.handle.net/1765/866

Waal, T. de, *Processing of Erroneous and Unsafe Data*, (co-) Promotor(s): Prof.dr.ir. R. Dekker, EPS-2003-024-LIS, ISBN: 90-5892-045-3, http://hdl.handle.net/1765/870

Wielemaker, M.W., *Managing Initiatives. A Synthesis of the Conditioning and Knowledge-Creating View.* (co) Promotor(s): Prof.dr. H.W. Volberda & Prof.dr. C.W.F. Baden-Fuller, EPS-2003-28-STR, ISBN 90-5892-050-X, http://hdl.handle.net/1036

Wolters, M.J.J., *The Business of Modularity and the Modularity of Business*, (co-) Promotor(s): Prof. mr.dr. P.H.M. Vervest & Prof.dr.ir. H.W.G.M. van Heck, EPS-2002-011-LIS, ISBN: 90-5892-020-8, http://hdl.handle.net/1765/920

Wijk, R.A.J.L. van, *Organizing Knowledge in Internal Networks. A Multilevel Study*, (co-) Promotor(s): Prof.dr.ing. F.A.J. van den Bosch, EPS-2003-021-STR, ISBN: 90-5892-039-9, http://hdl.handle.net/1765/347

The Rise of Regionalism

Regionalism has eclipsed the multilateral system as the 'fast track' for international economic restructuring. Within that framework, the Single European Market (SEM) and North American Free Trade Agreement (NAFTA) have emerged as the bi-polar core of the global economic system. Both agreements were sold to the public on relatively abstract terms, employing complex economic models as the basis for projected growth and increased competitive advantage. National governments at the time tended to take a relatively simplistic view of 'the firm' and ignore the strategic diversity among economic actors. Partly as a result, ten years into the 'Second Wave' of regionalism there are few uncontested conclusions as to its outcomes or significance.

Regional integration in Europe and North America was largely facilitated through the lobby activity of Western 'core companies': large, powerful firms that lead economic restructuring and operate with one foot in the political process. For Western core companies, regionalism has become the institutional framework of choice within which the struggle for the preservation and consolidation of their core positions is played out. Taking their spatial organization of production in 1990 as a baseline, this study is the first to systematically unravel the traditional macro-aggregated understanding of integration outcomes. The evidence shows that, despite the persistence of 'globalization' ideology, regionalism has fueled a diverse pattern of strategic migrations among core companies, particularly since 1995. The outcome is one of growing polarization between North American and European core companies, and consequently within an increasingly dyadic world economy.

ERIM

The Erasmus Research Institute of Management (ERIM) is the Research School (Onderzoekschool) in the field of management of the Erasmus University Rotterdam. The founding participants of ERIM are the Rotterdam School of Management and the Rotterdam School of Economics. ERIM was founded in 1999 and is officially accredited by the Royal Netherlands Academy of Arts and Sciences (KNAW). The research undertaken by ERIM is focussed on the management of the firm in its environment, its intra- and inter-firm relations, and its business processes in their interdependent connections. The objective of ERIM is to carry out first rate research in management, and to offer an advanced graduate program in Research in Management. Within ERIM, over two hundred senior researchers and Ph.D. candidates are active in the different research programs. From a variety of academic backgrounds and expertises, the ERIM community is united in striving for excellence and working at the forefront of creating new business knowledge.

ERIM
ERASMUS RESEARCH
INSTITUTE OF MANAGEMENT

www.erim.eur.nl

ISBN 90-5892-062-3