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Global, Local, or Regional? The Locus of MNE Strategies

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Abstract

This paper provides an overview of the main insights arising from the ‘regional strategy’ literature. It also develops the contours of a new, rich research agenda for future international strategy scholarship, whereby the region should be introduced as an explicit, third geographic level of analysis, in addition to the country-level and the global level. Regional strategy analysis requires a fundamental rethink of mainstream theories in the international strategy sphere. This rethink involves, *inter alia*, internalization theory, with its resource-based view and transaction cost economics components, as well as the integration (I) – national responsiveness (NR) framework.

INTRODUCTION

Rugman and Verbeke's (2004) *JIBS* article on regional versus global strategies of multinational enterprises (MNEs), and Rugman's (2005) subsequent book on regional multinationals have triggered a renewed reflection in international strategic management research on the locus of MNE strategies. Here, the focus has been on answering two questions. First, where do international business opportunities arise? Second, how do MNEs respond to such opportunities, given the objectives of exploiting—and further augmenting—their extant reservoir of firm-specific advantages (FSAs), thereby permitting sustained, profitable growth?

A common perception in the international strategy field, and in society at large, is that internationally operating firms pursue—or should pursue—'global' strategies in terms of scanning the world for business opportunities and responding to such opportunities with a broad geographic deployment of their 'non-location-bound' FSAs (Levitt, 1983; Friedman, 2006; Van Agtmael, 2007; Yip, 2001). However, the empirical evidence does not fully support this view (Verbeke, 2013). Even the suggestion that MNEs should be scanning the world, including peripheral host locations, to identify and absorb locally embedded resources (especially knowledge) and blend these with existing ones, i.e., engage in strategic asset seeking, as the foundation of new FSA generation (Doz et al., 2001), has been challenged based on the problems of bounded rationality (*BRat*) and bounded reliability (*BRel*)¹ inherent in such an approach (Verbeke and Kenworthy, 2008).

Rugman and Verbeke (2004), focusing on MNE foreign market success, observed that only nine firms from the Fortune *Global 500* (data from 2001) had actually achieved a balanced distribution of their sales across the globe. These nine firms included Canon, Coca-Cola, Flextronics, IBM, Intel, LVMH, Nokia, Philips and Sony. Perhaps more importantly than the

presence of only 9 global firms (with this number determined by the specific metrics adopted²) was the observation that the Fortune *Global 500* firms had the bulk of their sales in the home region, suggesting a limited ‘non-location boundedness’ of these large MNEs’ FSAs. In fact, 320 out of the 380 firms for which data were available, were solidly home-region based, with home-regional sales representing 80.3% of overall sales.

Rugman and Verbeke (2008) and Rugman and Oh (2012) then extended and updated this prior focus on sales to include the geographic distribution of assets, thereby confirming the results obtained for sales activities. The world’s largest MNEs have a limited deployment of foreign direct investments across value chain activities outside of their home region: 78% of assets were deployed in the home region and these were associated with 75.5% of overall sales (data for 2007).

These observations have prompted a lively debate among international business scholars. They also led to an entire new stream of research, including several subsequent empirical studies that challenged and extended this work (Dunning et al., 2007; Osegowitsch & Sammartino, 2008), and ultimately corroborated (with new methods and data) the main conclusion that MNEs do have a strong home region bias in their expansion patterns (Asmussen, 2009; Asmussen and Goerzen, 2013).

In this paper, we explore some of the key conceptual challenges that the above observations have prompted for international strategic management research. In particular, given the apparent importance of regional boundaries, we arguably must revisit some of the conceptual frameworks in international management that have become axiomatic in the literature and in business school curricula, such as internalization theory and the integration – national responsiveness (I – NR) paradigm. These are conceptual frameworks that address problems

associated with the orchestration of resources across borders and with economizing on spatial transaction costs in managing external business partners or the MNE internal network (Verbeke and Merchant, 2012).

In the next section, we briefly discuss the possible role of the region being a key locus for strategy formation, i.e., as a complement to the national and the global levels, building upon internalization theory. In the third section, we discuss in more detail the possible reasons for the relative absence of global diversification. We also address the challenges associated with trying to establish a linkage between geographic footprint and performance at the firm level. Finally, we assess the infusion of organizational elements such as regional head offices and regional value chains in the MNE to address the challenges posed by a geographic footprint extending beyond the home region. In doing so, we take on board the new thinking on regional strategy to assess how this might affect the classic I–NR framework, with a focus on providing substance to the so-called ‘transnational solution’ (Bartlett and Ghoshal, 1989).

THE REGION AS LOCUS OF INTERNATIONAL STRATEGY

As we indicated in the Introduction, recognizing the region as a key locus for MNE strategy formation has important research implications, and adding the ‘region’ to international business analysis requires a rethink of the strategic management models³ conventionally adopted by international business scholars. Mainstream international strategy research, drawing from the resource based view (RBV) component of internalization theory (Buckley and Casson, 1976; Rugman, 1981; Rugman and Verbeke, 2002 and 2005; Verbeke et al., 2014), builds on the observation that successful international expansion must be associated with a least some type of non-location bound FSAs. These are FSAs that can be transferred, deployed and exploited across

borders. Transaction cost economizing should then allow creating a governance context conducive to long-run value creation and value distribution, e.g., by guiding the governance mode(s) to be adopted in international business transactions⁴. Non-location bound FSAs can be embodied in final products (typically leading to exports), or shared across the MNE network (typically leading to foreign subsidiaries being established, whether in the form of wholly owned operations or equity joint ventures), or exploited through contracting with third parties (as is the case with licensing, production agreements, etc.).

Irrespective of how non-location bound FSAs are transferred, such FSAs can lead to three types of 'benefits of integration' (Rugman and Verbeke, 1992): economies of scale (from concentrating specific activities in one location), economies of scope (from sharing resources across borders, especially knowledge and governance-related resources such as shared accounting and ICT related practices), and economies of exploiting national differences (from distributing the value chain across borders and then coordinating these geographically dispersed activities).⁵

However, these three types of benefits are not easy to achieve in practice, at least not on the global level. Only in exceptional circumstances does global success materialize easily and rapidly. Such exceptional circumstances include both demand side and supply side components. At the demand side, an instant global interest from internationally dispersed customers for a niche market product, combined with low marketing mix adaptation requirements and low cost means of marketing and delivery, can increase the non-location boundedness of FSAs. At the supply side, an advanced technology or service offering, duly protected from competitive imitation, will have a similar effect (Hennart, 2014; Banalieva and Dhanaraj, 2013).

In most real-world cases, however, successful international expansion requires recombining extant resources with resources located in host countries, whether these resources are easily accessible through market contracts or held by resource owners in highly imperfect markets (Hennart, 2009; Verbeke et al., 2012 and 2014). In other words, *linking investments* (Rugman and Verbeke, 2005) must typically be made by the MNE to blend extant resources with locally accessible ones held by host country resource owners, thereby driving the creation of new, location-bound FSAs in host countries, i.e., an ability to be nationally responsive in critical areas of the value chain.

The above analysis suggests that a successful international strategy in terms of achieving profitable growth entails careful selectivity as to where and how the firm should expand, and it is here that the regional dimension of international strategy comes in, as shown in Figure 1.

Insert Figure 1 about here

The horizontal axis of Figure 1 shows the *geographic locus of international expansion opportunity*. This locus can refer to a single host country, a region, or it can be global (geographically unconstrained). The vertical axis shows the *geographic reach of non-location bound FSAs*. Here, the ‘non-location-boundedness’ or geographic reach of the MNE’s FSAs can be limited (e.g., to a proximate country), or it can be region-bound, or it can be global (geographically unconstrained).

Mainstream international strategy thinking has focused mainly on the bottom left and the top right portions of Figure 1, with the former emphasizing that distance between countries still matters (cf. Ghemawat, 2001) and the latter drawing attention to the opportunity and need to

develop global strategies (Tallman and Yip, 2001). The question then arises as to the significance of the middle section in the matrix, which has been usefully designated as the sphere of ‘semi-globalization’ (Ghemawat, 2007). The concept of the region, broadly understood as a grouping of countries that are relatively similar to each other *and* relatively dissimilar to countries in other regions, naturally belongs in this sphere. There are two broad research approaches to assess semi-globalization and the role of the region in MNE strategy. As elaborated in the following sections, both of these approaches highlight the relevance of particular MNE positions in the middle section of Figure 1.

With the *first approach*, FSAs are viewed as region-bound, in the sense of having limited exploitation potential outside of the home region: both the strength of the MNE’s FSAs and the spatial transaction costs associated with their transfer, deployment and exploitation are moderated by regional boundaries. This approach has implications for both the positive (predictive) and the normative strands of international management research. In terms of predictive research, the conceptual challenge is to explain the simple observation that home-region diversification is the prevalent mode of internationalization, even among most of the world’s largest firms. In other words, home-region diversification is ‘preferred’ over global diversification in most ‘real world’ situational contexts (Rugman and Verbeke, 2004 and 2005; Rugman, 2005; Rugman and Oh, 2008). On the normative level, firms may have ‘over-diversified’ geographically, especially when expanding beyond the home region, and are expected to exhibit a weaker performance as a consequence. Here, the main challenge is to explain why such overextension and negative effects would be commonly observable and across time. Presumably, both benchmarking the firm’s geographic footprint against that of rivals, and internal learning within the MNE, would allow avoiding or mitigating costly geographic

expansion mistakes. Some systemic biases, however, such as overestimating the inter-regional transferability, deployability and exploitation potential of FSAs may be instrumental to lower performance outside of the home region (Banalieva and Eddleston, 2011; Mohr et al., 2014).

The *second approach*, which is an extension of the first, does not have as its main emphasis the absence of global diversification or the performance implications thereof, but rather focuses on how firms that have already expanded into host regions (in spite of the challenges described above, and possibly with a modest footprint), adapt to a world where regional barriers to full, global integration continue to exist. The limited possibilities are acknowledged for many firms to earn ‘global’ scale economies, scope economies, and benefits of exploiting national differences. However, ‘solutions’ are explored in the form of regional responsiveness, including the MNE’s propensity to infuse regional components in its organizational structure and operational functioning (Ghemawat, 2005; Piekkari et al., 2010; Alfoldi et al., 2012; Rubera et al., 2012).

In the next section, we explore the above two approaches: we will first discuss the issue of many MNEs limiting their footprint to the home region, and we will then turn to the analysis of regional components in the MNE’s organizational structure and functioning.

RESEARCH PERSPECTIVES ON THE ROLE OF THE REGION IN INTERNATIONAL STRATEGY

Internalization theory and regional boundaries

Firm-Specific Advantages and Regional Strategy

As noted above, the empirical evidence points to the relative absence of global firms. Such absence means more than simply geographic proximity driving both higher volumes of FDI

and more international economic activity in general, whereby distance between countries would be treated as a continuous variable, as in the classical ‘gravity model’. A regional strategy research agenda arises precisely because of substantial discontinuities of distance at the regional boundary (Asmussen, 2012; Flores et al., 2015). Here, the distance between countries forming a region and those outside of it represents a quantum leap or ‘spike’ as compared to intra-regional distance (see Rugman et al., 2011a).⁶ The reasons why distance from a firm-level perspective is lower when operating in the home region as compared to host regions, can be manifold. Geography clearly matters here—for example, regions may be separated by vast oceans or scarcely populated land masses, as well as large time zone differences, known to inhibit MNE coordination and FDI (Stein and Daude, 2007; Espinosa and Carmel, 2003). In addition to geography, however, cultural, economic, and institutional elements can play equally strong roles, and, most importantly, it is the inter-relatedness among these dimensions that causes a spike in *compounded distance* at the regional border. For example, a regional trading block or common currency will directly reduce intra-regional, institutional distance for insiders. In turn, overarching regional institutions can, through the freer flow of human and financial resources as well as goods and intellectual property, foster more commonality in cultural values relevant to business and also reduce economic distance. Stronger economic commonalities (e.g., shared distribution practices) are likely to increase demand for new regional infrastructure (such as the Trans-European Networks in the European Union), thereby reducing the impacts of geographic distance on business. In other words, a virtuous cycle occurs of interrelated distance dimensions being reduced.

Outsiders to the region face a compounded distance ‘spike’ relative to the insiders. In turn, insiders venturing outside of their home region face an inter-regional distance spike as

compared to the prevailing distances between countries in the home region (Flores et. al, 2015). Importantly, compounded distance can express itself in relationships with multiple external actors, especially those holding requisite complementary resources, and in internal relationships, within the MNE, for example in head office – subsidiary relationships: higher compounded distance typically requires more complex resource bundling processes (Verbeke and Kano, 2016).

To the extent that the comparatively lower intra-regional distance has been ‘crafted’, for example as the result of regional trade and investment agreements such as the North-American Free Trade Agreement (NAFTA) or the European Union/European Monetary Union (EU/EMU), barriers to profitable growth may thus be raised for regional outsiders relative to insiders. However, the magnitude of the business opportunity, elevated from the country level to the regional one, may also increase for the outsiders (Arregle et al., 2013). The locus of some business opportunities thus shifts from the left to the centre of the horizontal axis of Figure 1.

In terms of company-level strategic responses, regional business opportunities provide incentives to ‘upgrade’ extant FSA reservoirs via a myriad of different strategies, so as to achieve higher scale and scope economies, and benefits of exploiting national differences at the regional level (Rugman et al., 2011b). In other words, location-bound FSAs at the bottom of Figure 1 can be ‘upgraded’ to become region-bound ones, positioned in the middle of the vertical axis of this Figure. Here, regional integration at the firm level prevails, as has been observed in Europe, where the Single Market has led many large MNEs to replace their country-level distribution operations by European Distribution Centres (EDCs). It has also been observed that MNE operating mode choices are altered, because in cases of far-reaching economic and

political integration such as the EMU, national institutional risk becomes irrelevant to operating mode selection by insider firms (Verbeke, Hillemann and Oh, 2015).

Conversely, MNEs commanding FSAs with supposedly global reach can now ‘fine-tune’ such FSAs further, i.e., engage in some form of regional responsiveness, again leading to region-bound FSAs with stronger actionable potential than before to capture regional scale and scope economies and benefits of exploiting national differences within the region. Adaptation to the requirements of a particular geographic area may not have been viewed as feasible or economically viable before, but now becomes feasible and viable because of regional integration, thereby potentially allowing an increase in size of the firm’s footprint in the relevant host region⁷. A shift occurs from the top to the middle of the vertical axis of [Figure 1](#).

Here, it should be recognized that past research with its focus on comparing home regional sales and assets with equivalent data for host regions does not take into account the possibility that MNEs may have a different propensity to use alternative operating modes in host regions, where, e.g., licensing agreements or manufacturing contracts may play a more important role. In this context, regional strategy may be more important for some value chain activities than other ones, and it is thus clear that only a full value chain analysis, including all internal and external ‘contracts’, would allow assessing the role of the region in overall operations (Rugman et al. 2011b; Mudambi and Puck, this issue). A mere focus on the production function (as proxied by, for example, asset volumes and manufacturing contracts) would typically cover mainly the resource seeking and efficiency seeking strategic motivations for international expansion, whereas a sole focus on sales would do justice only to the market seeking strategic motivation.

The above analysis of regional strategy fits well with the RBV component of internalization theory, which points to the limits of international diversification (Narula and Verbeke, 2015). Firms' resource bundles typically lead to more profitable growth opportunities in the home region than in host regions, because of the comparatively stronger similarity between the home country environment and that of other countries in the home region (Rugman et al., 2011a). This argument is similar to that in the product sphere with profitable growth supposedly easier to achieve through related diversification than through unrelated diversification (Jones and Hill, 1988).

Spatial Transaction Costs and Regional Strategy

Internalization theory does not only have an RBV dimension, but also an equally important TCE dimension, whereby FSAs must be protected through economizing mechanisms (Narula and Verbeke, 2015). The question then arises whether a home region strategy, built on region-bound FSAs, could be interpreted as the outcome of such economizing. Given imperfect information and limited information processing capacity, seeking profitable growth inside the home region, i.e., inside 'low compounded distance' countries, would appear consistent with the need to economize on bounded rationality (*BRat* or 'scarcity of mind'). Lower compounded distance, meaning more intra-regional similarities both among country environments and among the configurations of firm-level activity sets conducted in the relevant countries, reduces spatial transaction costs and fosters a home-region strategy approach. Such similarities at the level of the environment can include elements as varied as regional commonalities in business taxation and intellectual property rights protection. At the firm-level, intra-regional similarities can range from quasi-identical human resources management practices to after-sales service routines for customer support. As a result, bounded reliability challenges (*BRel* or 'scarcity of making good

on open ended promises’) inside the home region can also be substantially reduced vis-à-vis outsider regions (Verbeke and Greidanus, 2009). Here, adopting ‘proven’ managerial routines and decision making heuristics can also be much more effective than in high compounded-distance environments.

Selectivity in internationalization, with a focus on the home region, is thus fully consistent with mainstream internalization theory (Rugman and Verbeke, 2005; Verbeke and Kano, 2012). Many firms refrain from attempts at globalizing, i.e., seeking profitable growth through expanding across the world, and instead try to focus on home country/home region success. The first challenge when trying to achieve profitable growth in host regions is thus to bundle extant FSAs with requisite resources in these host environments (an RBV related issue). The second challenge in host regions is that the spatial transaction costs and related, necessary linking investments are substantially higher than in the home region, and the effectiveness thereof much more uncertain, because of *BRat* and *BRel* challenges (a TCE related issue).

The Dangers of Geographic Overstretching

The mechanisms outlined above have implications not only for firm-level choices in terms of expansion outside the home region (and hence for the existence or absence of global firms), but also for the performance of those firms that do choose substantial global expansion. A large empirical literature exists on the linkages between multinationality and performance (M - P). Overviews of the methodological soundness of this empirical work paint a rather dim picture of the state-of-the-art (Verbeke and Brugman, 2009; Verbeke and Forootan, 2012). In some cases, neither multinationality, nor performance, are measured appropriately and the linkages between both concepts tend to neglect or at least downplay critical issues such as endogeneity and reverse causality. The methodological weaknesses of many empirical studies explain at least

partly the absence of any definitive conclusion on the direction and magnitude of M - P linkages, if such linkages could reasonably be assumed to exist in the first place (Hennart, 2011). However, the introduction of a regional dimension in the M - P literature opens the door to a new empirical research stream.

If it can reasonably be assumed that in most cases inter-regional expansion will be fraught with *BRat* and *BRel* problems beyond those associated with home regional expansion, the danger exists of ‘overstretching’. Overstretching would reflect ‘mistakes’ such as MNE managers’ exaggerated belief in the transferability, deployability and profitable exploitation of allegedly non-location bound FSAs, meaning that these FSAs are really home-region-bound. Overstretching could also mean underestimating the magnitude of the linking investments needed to meld extant resources with new ones, as a precondition for new FSA creation. Finally, overstretching could simply mean that the geographic scope of the firm’s activities is too broad for efficient governance to occur, given that the existing governance mechanisms were designed to address only limited compounded distance. Here, the internal, spatial transaction costs related to global expansion are underestimated.

Overstretching results in a reduction in performance, at least in the short and medium term. In the long term, the expectation would be that overstretched firms would correct their excessively high level of geographic diversification. A potentially promising angle in this context is the analysis of the trade-offs between increasing product diversification versus inter-regional geographic diversification, since governance problems related to *BRat* and *Brel* may arise in both cases.

In line with mainstream work on M - P, the extant research on the linkages between the regional dimension of multinationality and performance has been equally inconclusive, with

some studies finding evidence of geographic overstretching and showing the performance superiority of home-regional expansion (Qian et al, 2010), whereas other ones have demonstrated the superior performance of globally diversified firms (Delios and Beamish, 2005).

Oh and Contractor (2014) applied 'S-curve' thinking to study the M - P relationship in a regional expansion context. With S-curve thinking, performance is supposed to go down in a first stage of international expansion, *inter alia* because of spatial transaction costs. In a subsequent, second stage with a focus on home-region expansion, the M - P relationship is hypothesised to be positive, *inter alia* because of easily achievable scale and scope economies, as well as benefits of exploiting national differences. However, further expansion beyond the home region could negatively affect performance, since "coordination and governance costs escalate due to the increasing complexity and diversity of knowledge, business practices and consumer tastes that the company encounters" (Oh and Contractor, 2014, p. 46). The important question raised by this work is whether the predicted occurrence of inter-regional overstretching can be avoided.⁸

In line with Shaver (1998), it is reasonable to assume that firms engaged in international expansion beyond their home region do so because of the non-location bound FSAs they command, which is a cornerstone of mainstream internalization theory (Buckley and Casson, 1976; Rugman, 1981). The challenge facing scholars performing empirical work on this issue is that the 'value' of FSAs, when deployed beyond the home region, does not remain stable. On the one hand, knowledge-based FSAs are supposed to confer economies of scope, but these may be subject to decay in host regions, as explained above, and MNE managers may have incorrectly anticipated such decay. More specifically, the extant FSA reservoir may only achieve its predicted, international value-creating potential, subject to novel resource

recombination in host region markets, whereby higher compounded distance can make such recombination more difficult to anticipate correctly and to implement effectively (Verbeke and Kano, 2016). On the other hand, a global network of subsidiaries can confer an option value to the MNE, meaning that the MNE can now switch the location of economic activities as a function of unexpected changes in exogenous parameters such as exchange rates, fiscal policies, growth rates, etc., all of which may have a regional component (as in the case of the European Monetary Union). In other words, an inter-regional footprint may give the MNE more flexibility in its decision-making and thereby confers value when regions evolve differently over time.

Because of *BRat*, both the magnitude of spatial transaction costs (and associated requisite new resource recombination) and the option value of particular decisions to enter a specific region, may only become apparent *ex post*, after initial investments in the region have been completed (Verbeke et al., 2015). Importantly, the effects on performance of inter-regional diversification will at least partly be determined by managerial biases (typically in the sense of underestimating spatial transaction costs and overestimating the global reach of FSAs), by unpredictable external shocks, and by differences in the macro-level evolution of the home versus host regions. For example, Chang et al. (2015) found that the option value of global diversification was positive after the 2008 – 2009 financial crisis, but at the level of the individual firm, any such option value is determined by the MNE's managerial capability to take advantage of governing a global network (e.g., through operating effective inter-regional coordination and arbitraging mechanisms).

The more general point is thus that M - P studies embracing a regional dimension face largely the same methodological challenges as past studies in this area that only made a distinction between the home country and foreign nations, to determine the level of

multinationality, and to establish any link thereof with performance. New hypotheses with a regional dimension can be formulated, and the short/medium term situational performance effects of both regional overstretching and network options can reasonably be hypothesized. However, the long-term expectation remains that no universal performance differences should result from mere variations in geographic diversification, in this case with a focus on the region. Here, elements such as endogeneity, reverse causality and the impact of external shocks on the MNE network systematically need to be taken into account in empirical studies (Verbeke and Forootan, 2012).

Regional Strategy, Structure and Organizational Systems

The above analysis has focused mainly on explaining many MNEs' relative home-region orientation and the reasons for the typical absence of a balanced spread of activities across the world (whereby a balance would indicate the ability to emulate home-region success in host regions). Nevertheless, many MNEs do have at least some geographic footprint outside of their home region. Acknowledging the overwhelming empirical evidence on the important role of both home-regional market opportunities and region-bound FSAs as an input for strategy formation, does suggest the need for selectivity in internationalization. However, this does not imply that barriers to inter-regional expansion remain invariably very high over long time periods. In fact, on the *environment side*, host region integration can provide attractive opportunities for outsiders to exploit their FSAs, *inter alia* if regional regulatory controls are kept low, see Arregle et al. (2013). These authors usefully suggest that a first FDI in a host region that includes linking investments to combine extant FSAs with resources in the host region, can act as an expansion platform. This platform reduces the outsider's initial *BRat* and

BRel challenges when engaging in subsequent FDI decisions. On the *internal organization* side, subsidiaries' absorptive capacity in the host region may increase as regards effectively receiving and subsequently deploying and bundling extant FSAs with host region resources. Not only does resource accumulation occur, but information gained through the first entry in a host region can reduce the internal organizational *BRat* and *BRel* problems arising in all subsequent entries in the region. Furthermore, as noted by Rugman and Verbeke (2005), inter-regional investments often occur in more upstream activities because all relevant economic actors (external research labs, component suppliers, logistics providers; employees; etc.) can make *ex ante* credible commitments to establish R&D, production or logistics operations in a particular host location. Such credible commitments, and the associated agreements on the subsequent distribution of created value, largely eliminate *BRat* and *BRel* challenges (or mitigate the negative effects thereof), and imply that these value chain activities can more easily be conducted outside of the home region (Mudambi and Puck, this issue).⁹ We describe below the organizational implications of the above dynamics for inter-regional, profitable growth.

Assuming that economic activities are internalized in multiple regions, there is potential for a regional organizational dimension. In fact, MNEs that have been successful in their home region with a regional strategy are more likely to try to emulate such success in other large, regional markets, with the extant home region-level routines and elements of organizational structure easier to adapt than if the firm had to craft these without prior home-region-level experience in this matter. In other words, home-region organizational components can have generative effects in host regions (somewhat similar to the easier international adoption of multidivisional organization after its successful domestic implementation). Two of the most important organizational components linked to regional strategy are regional head offices and

regional value chains. Assuming the possibility of deploying effectively these types of regional organizational arrangements by the MNE, the question arises how prescriptive international strategy frameworks such as the I – NR framework could be augmented so as to keep their relevance to international business scholarship and managerial practice.

Regional head offices

Regional head offices can either be specialized units dedicated to critical headquarters functions only, or operating subsidiaries to which regional head office functions have been delegated by the corporate head office (Lasserre, 1996; Piekkari et al., 2010). Establishing regional head offices is somewhat similar to creating multidivisional structures to reduce *BRat* and *BRel* problems, by allowing the corporate head office to specialize in key, overarching strategic management domains and giving divisional leaders operational autonomy over decision making in specialized product areas. In this case, the regional head office is supposed to alleviate *BRat* and *BRel* problems by specializing its head office functions in favour of narrow region-specific substance matter (Yeung et al., 2001). More specifically, it is through the regional head office that coordination can occur among operations located in the various countries inside the region, and that decisions can be made on requisite linking investments to complement extant non-location bound FSAs with location bound ones (Enright, 2005a; Enright, 2005b). The coordinating role of the regional head office is strongly related to the concept of ‘regional strategy’, which we discuss below.

Regional head offices are also particularly well equipped to engage in monitoring of country operations within their region: they will face fewer *BRat* problems as compared to the corporate head office when trying to make sense of the performance metrics for the various country operations and they are also more likely to be able to maintain reliability of these

operations (e.g., by curbing opportunism) because of their proximity to them and the related reduction in information asymmetries.

Regional head offices play an important role in giving visibility to an MNE's dispersed presence in a region, and may be instrumental to transferring knowledge among units located within this region. At the upstream end, they can be useful especially in implementing, but also fine-tuning central routines. At the downstream end, they can be useful for example in strengthening company brand names, throughout the region. Here, region-bound FSAs should be considered valuable, and potentially long-term, strengths. Region-bound FSAs are therefore not an 'imperfect' FSA type as compared to those with unlimited geographic coverage, whereby region-bound FSAs would be a mere stepping-stone towards the latter (cf. [Figure 1](#)).

Specific attention should be devoted to regional head offices of emerging economy MNEs, since these can be instrumental in identifying, accessing and absorbing new, requisite non-location bound knowledge in host-region environments that may be sorely lacking inside the firm. In addition, regional head offices, when set up in the home region itself, could be viewed as a tangible expression of a 'springboard strategy' (Luo and Tung, 2007), signalling the firm's continued commitment to expanding in the home region and showing the presence of an international management capability to serve key stakeholders in that region. Home region head offices can also be located in countries known for particular quality features (e.g., Japanese product quality), again to give a signal to the market that the firm highly values such features, and to eliminate potential negative quality perceptions associated with the MNE's home country.

However, regional head offices do come at a cost. *First*, in terms of *BRat*, one more layer is created between the MNE's corporate headquarters and the actual locus of addressing operational challenges, typically in individual, host country subsidiaries. As a result, the

likelihood that local problems in country level subsidiaries will ever become visible to the corporate headquarters' level, is actually reduced, meaning that the *BRat* challenges faced by the corporate headquarters are increased. *Second*, in terms of *BRel*, the presence of multiple units to which regional head office functions are allocated, is fraught with governance challenges. For example, regional head offices may give priority to the operations in the country where they are located at the expense of other countries in the region. They may also provide biased information, both to the corporate headquarters to which they report and to the country-level operations they are supposed to support with various services in their region.

Regional Value Chains

Linked to the presence of regional head offices, is the creation of regional value chains. Suder et al. (2014) have noted, e.g., that “the locational interdependence of developed and less - developed countries across the region leverages on the heterogeneity of location-specific advantages within the region.” These authors studied the rise of regional value chains in East Asia since 1990, and found widening and deepening trade relationships among East Asian countries. Japan still appeared as dominant partner in regional production systems, but based on sophisticated input – output analysis, the authors concluded (Suder et al., 2014: 408):

“By 2005, almost all Asian developing countries enhanced their presence in international trade in this region. There are two notable features: the increasing interaction and complexity between China, Korea, Japan and Taiwan, and the increasing interdependence between East Asia and ASEAN.”

If some MNEs establish regional head offices to manage their internal operations in the various regions more effectively, in terms of economizing on *BRat* and *BRel*, then it can also be assumed that the observed rise at the macro-level of regional value chains would translate into equivalent chains at the firm-level, with low interactions among individual, regional value chains

(somewhat similar to creating specialized product divisions, subsequently leading to low interactions among these divisions, which may merely have in common a number of core, non-location bound FSAs).

Augmenting international strategy frameworks

As noted above, one of the purposes of the regional head office is to implement a regional strategy, which emphasizes coordination within each region and orchestration of the regional value chain. The question is how such a strategy can be reconciled with conventional organizational prescriptions in the international management literature. The framework most often used in strategy textbooks to describe alternative, international strategy options and to prescribe the ‘optimal’ organizational approach associated with each of these, is the classic I – NR framework, which we introduced earlier and which is widely adopted in business schools to analyze real-world managerial challenges facing MNEs (Prahalad and Doz, 1987; Bartlett and Ghoshal, 1989; Verbeke, 2013). However, as this framework essentially builds upon a local – global distinction, it leaves no explicit role for the region. Given the availability of regional organizational components, as described above, it would appear appropriate to assess how the regional level can moderate the tensions between I and NR.¹⁰

The I - NR framework in its original formulation is essentially an application of contingency theory, which holds that no universal set of organizational choices will lead to optimal outcomes for all firms; instead, performance is determined by the *fit* between the environment in which the firm operates on the one hand, and the strategy and organizational approach it adopts on the other (e.g., Lawrence and Lorsch, 1967). As illustrated in [Figure 2](#), the I - NR framework builds on this logic, defining the MNE’s environment along two dimensions. Pressures for global integration are driven by interdependencies across countries. These include, *inter alia*,

economies of scale and scope, which require standardization and coordination respectively of the MNE's international activities in order to reap global cost efficiencies. Pressures for national responsiveness, on the other hand, are driven by country-to-country differences in customer preferences, government regulation, culture, institutions, and other external parameters. They imply that tailoring the MNE's activities to each country environment can bring adaptation benefits including, for example, higher demand and the ability to charge higher prices for the MNE's products.

Depending on whether the pressures for I and NR are high or low, the MNE's environment can be positioned in Figure 2. Based on organization theory and case studies of both successful and unsuccessful MNEs, Bartlett and Ghoshal (1989) prescribed optimal strategies and related organizational approaches for various environments: 'global', 'multinational' and 'transnational' (note that this simple framework neglects the strategy of exploiting national differences or arbitrage, see our discussion above).

Insert Figure 2 about here

With the I - NR framework, it is straightforward how MNEs should respond when integration pressures are high and responsiveness pressures low, in quadrant 1 of Figure 2. They should pursue a 'global' approach with geographically concentrated value chain activities, standardized products and processes, and decision making centralized in global functions and in the head office, thereby leading to economies of scale.¹¹ For example, the iPhone is produced and sold in essentially the same specification in all countries, enabling Apple to reap substantial scale economies in R&D, procurement, and production. Similarly, when responsiveness

pressures are high and integration pressures low, in quadrant 4 of [Figure 2](#), MNEs should pursue a ‘multinational’ approach characterized by geographically dispersed activities, locally adapted products and processes, and local autonomy delegated to the national subsidiaries. Hence, 95 percent of the products stocked by global retailer Carrefour are national products, reflecting the importance of local cultural tradition in food and beverage consumption.

However, what is less clear in this framework is how MNEs should approach the scenario whereby the industry is faced with pressures for *both* high integration and responsiveness simultaneously. In other words, what is the actual content of the ‘transnational’ approach in the top-right quadrant 3, of [Figure 2](#), in terms of optimal strategy and organization? In part, this ambiguity arises because the substance of global versus multinational strategies to some extent is contradictory—for example, a product cannot be simultaneously standardized and locally adapted—and therefore the transnational strategy cannot simply be a sum of the two simple strategies. This is a conundrum that has led international business scholars to examine the nature of the ‘tensions’, or even ‘trade-offs’, between I and NR (e.g. Doz and Prahalad, 1991; Hannon et al., 1995; Devinney et al., 2000; Asmussen, 2007; Meyer et al., 2011). Some commonly mentioned, organizational design solutions adopted by MNEs include evenly balanced matrix structures, normative integration, and flexibility to adapt the strategy and structure of the firm, its individual business units, and even its functions, depending upon the industry context (Bartlett and Ghoshal, 1989).

The authors developing this literature did not explicitly preclude the possibility that both sets of pressures might operate as continuous variables, e.g., on the production cost dimension. For example, if one conceptualized the strength of manufacturing economies of scale as the average cost difference between producing on a national scale and producing on a global scale,

this cost difference could in principle take on a range of ‘intermediate’ values between high and low. Similarly, country diversity could be operationalized as the size of the economic ‘penalty’ (e.g. lower sales) that the MNE would incur if it were to deviate from host country national standards (e.g. trying to sell a ‘global’ product that does not meet local customer preferences), and this penalty could again take on a number of ‘intermediate’ values, rather than simply being high or low.

The above intermediate scenarios have not been developed in detail in the extant literature, neither conceptually, nor empirically, and—crucially—the region was never clearly acknowledged as the underlying reason for the presence of intermediate integration and responsiveness pressures. However, we can incorporate the region as an intermediate point on each of the two axes in the I - NR grid. As explained above, one of the central tensions in this grid is that between economies of scale on the one hand, and benefits of national responsiveness from adapting to customer preferences on the other. This tension provides a useful setting within which to test the impact of the regional level, which we do below.¹²

In an early review of the I – NR literature, Kobrin (1991, p. 17-18) explained that global integration enables MNEs to achieve “benefits from producing at optimal economic scale and from amortizing research and development cost over a broader base” and “larger, more efficient production runs, higher volume distribution networks, and support of higher levels of research and development”. The implication is that when MNEs produce one standardized product for the global market (as opposed to having different products for each individual market), they obtain scale economies in the form of lower unit costs, for example because they incur lower R&D cost per unit sold (cf. the iPhone example above). Consistent with this view, Kobrin (1991)

operationalized global integration pressures as the relationship between the economies of scale in industry and the size of the market, as shown in Figure 3.

Insert Figure 3 about here

Figure 3, included here for illustrative purposes only, reflects the simple case of a firm facing three different scenarios in terms of the average cost curve of the industry, with this firm manufacturing a single standardized product. As the firm produces a higher quantity of this product, its average costs go down for the reasons described by Kobrin (1991) above. Minimum Efficient Scale (MES) is defined as the point at which these scale economies are exhausted, and no additional average cost reductions can be gained by increasing output. An important question in terms of strategy is then whether the size of individual national markets is sufficient to allow the firm to achieve the MES prevailing in its industry. The dotted line captures a scenario whereby any economies of scale are indeed exhausted at the national level. In such an industry, it is cost-efficient for the firm to develop and manufacture a unique product for each of the countries in which it operates, as it can still achieve the lowest possible cost (denoted AC_{MES} in the figure) within each country. In contrast, the solid black line captures a scenario with global economies of scale: if the firm does not produce on a global scale, it will not achieve the MES and hence it will be at a cost disadvantage as compared to firms that do.

The contrast between the two black lines can be used to understand the vertical axis of the I - NR framework. If there are only national economies of scale to be gained, integration pressures are by implication low and hence a 'multinational' approach becomes feasible. In

contrast, if there are global economies of scale to be gained, this implies that integration pressures are high and a 'global' approach may become attractive.

Since the region is by definition larger than one nation, but smaller than the World as a whole, it becomes a natural candidate for moderate MES positions, as represented by the gray line in Figure 3. With *regional economies of scale* in a particular industry, a single nation will still be too small to allow firm-level, cost-efficient production, but the region is sufficiently large for the MES to be achieved, whereas global scale manufacturing does not lead to significant, additional cost advantages. In such an industry, the firm would therefore have an incentive to standardize its products within each region in which it operates.

However, the 'optimal' geographic level on which to pursue standardization also depends on the other axis, namely the national responsiveness pressures in the industry. National responsiveness pressures can be defined as "industry forces that necessitate local context-sensitive strategic decisions" (Roth and Morrison, 1990, p. 543). In managerial practice, national responsiveness can be triggered by many different parameters. For example, in order to assess empirically these pressures in different industries, Ghoshal and Nohria (1993) used two indicators: advertising intensity and a survey instrument capturing government regulation. The former could be interpreted as a proxy for the 'cultural intensity' of the product and thus for the extent to which consumer preferences vary across countries (for example, advertising intensity is high in the food and beverages industry, cf. the earlier Carrefour example). The latter indicator reflects the importance of government in shaping local responsiveness pressures. For example, while pharmaceutical products typically lack cultural content, the pharmaceutical industry is subject to intense, government-driven local responsiveness pressures as producers are forced to perform locally adapted clinical trials of their products.

However, as was the case with integration pressures, it is apparent that responsiveness pressures, irrespective of their source, increasingly come from the regional level. For example, standards are being imposed regionally in an effort to reduce technical barriers to trade within regions (Brenton et al., 2001), and the promotion of internal regional markets for goods, services, and labor may lead customer demand to become more homogenous within regions than across them (Rugman and Verbeke, 2005). With these developments in mind, we can conceptualize the regionally ‘spiky’ world that was discussed in earlier sections of this paper, with regions that are different from each other but relatively homogenous internally. Corresponding to this scenario is the ‘regional’ product strategy, which adapts itself to the particularities of each region (but standardizes within them), thereby avoiding the demand penalty of a ‘global’ strategy.

Note that an MNE might still choose a ‘global’ approach, even in the face of substantial responsiveness pressures, if it estimated the magnitude of the benefits arising from global scale economies to outweigh the demand penalty from a lack of adaptation. Similarly, it might choose a regional approach in spite of substantial intra-regional diversity and pressures for local adaptation, to achieve regional economies of scale. We therefore need to combine scenarios measuring integration benefits, as shown in [Figure 3](#), with scenarios estimating responsiveness benefits, as discussed above, to describe a ‘complete’ contingency model, see [Figure 4](#). With three possibilities on each axis, [Figure 4](#) shows the optimal MNE response within different types of environments.

Insert Figure 4 about here

First, we can see that introducing the region and the possibility of a regional approach to strategy and organization does not alter the conclusion for the two ‘extreme’ types of environments, namely the ‘global’ and ‘multinational’ environments. If the ‘world is flat’ and economies of scale can be gained at the global level, it will still be ideal for the firm to pursue a ‘global’ strategy with standardized products. If consumer preferences vary by country and scale economies are exhausted at the national level, the ‘multinational’ strategy with locally adapted products prevails.

However, the central space in the matrix is taken by a new, intermediate ‘semi-globalized’ state of the world, e.g., in the middle cell of the matrix, where both responsiveness pressures are integration pressures are regional. Here, a ‘regional’ strategy is optimal. No substantial additional scale economies are gained by standardizing beyond the level of single region. Similarly, little is gained by adapting below the regional level for the different countries within each region.

However, ‘regional’ strategy is not only relevant in a ‘purely’ regional world—it also appears outside of the middle regional cell and even in the top-right cell where no regional element is present in the environment. What this suggests is that a ‘regional’ strategy may be a ‘best available’ response to a transnational environment, located between the two extremes of the ‘global’ and ‘multinational’ approaches, because it effectively balances the conflicting forces for I and NR, and is a tool to achieve both simultaneously. Even if there are local responsiveness pressures within each region, the regional approach can improve the firm-level response to these pressures, because it will at least accommodate inter-regional differences. Similarly, even if there are global economies of scale to be reaped, a ‘regional’ strategy can improve integration by obtaining, if not all of these economies, then at least a significant part of them. For example,

suppose that the industry cost structure is described by the solid black line in [Figure 3](#), in which there are global economies of scale and the MNE can only obtain the lowest average cost (AC_{MES}) by moving all the way down the global cost curve and produce a standardized product on a global scale. However, it can obtain *almost* as low a cost level by producing a regional product, in which case it moves only some of the way down the global cost curve, to the point at which it obtains costs of AC^* .

The implication of this is that having a regional product will be less cost-efficient than having a global product will (because it is produced in lower quantities), but not by much (in the figure, the difference between AC^* and AC_{MES}), and this small difference in costs may be more than outweighed by the benefits of having a product that is better adapted to the unique characteristics of the region. In other words, if the ‘regional’ strategy allows achieving most of the integration and national responsiveness benefits in industry, while sacrificing only a little of each, it can be superior to the alternatives of global integration and national responsiveness. For example, Google’s Android One phone is targeted primarily at the Asian market, which has now become large enough to support development of regional smartphone models, and at the same time differs from Europe and North America on key demand characteristics like purchasing power and requested features—which is why merely ‘recycling’ smartphone designs from these markets have proven difficult for most vendors.

The above analysis can be interpreted as providing actual substance to the otherwise somewhat elusive ‘transnational’ approach to strategy and organization. This is consistent with anecdotal evidence suggesting that firms in ‘transnational’ industries, such as pharmaceuticals or automobiles, use regional strategies to balance strong and conflicting demands for integration and responsiveness—for example, the way in which Toyota and Honda build their product

portfolios around regional variants of their car models. We have thus infused the notion of the region in the simple I – NR dichotomy, and have highlighted the impact of the region on the conventional trade-offs between ‘global’ and ‘multinational’ strategies. In practice, there may be more sophisticated trade-offs to be made, such as between an integration strategy largely focused on economies of scope (Bartlett and Ghoshal’s (1989) ‘international’ strategy, with foreign operations being replicas of home country operations, mainly engaged in knowledge exploitation) and an integration strategy aimed at exploiting national differences (an approach neglected by Bartlett and Ghoshal). Still, similar tensions exist for these two integration benefits (beyond scale economies). Hence, the potential for economies of scope may be smaller, but easier to achieve on the regional level where compounded distances are lower and coordination across countries thus become easier. Similarly, the exploitation of national differences can take place through regional value chains as described above—a strategy that perhaps limits the extent to which national differences can be exploited, but also economizes on the costs (e.g. transportation costs and spatial transaction costs) of exploiting them.

Developing integration strategies to exploit national or regional differences typically entails the rise of centres-of-excellence within and across regions. Birkinshaw et al. (1998) predict under which circumstances local subsidiaries will make a contribution to MNE FSAs. Building on this work, Frost et al. (2002) identify the location-specific parameters determining whether a ‘centre of excellence’ will emerge in a particular location. In this context, Rugman and Verbeke (2001) coined the term “subsidiary-specific advantage”. Firms might thus try to tap into ‘regional diamonds’ by sourcing specialized location-specific resources (Asmussen, Dhanaraj, and Pedersen, 2009) and combining these with internally transferred knowledge (Asmussen, Foss, and Pedersen, 2013; compare with Mudambi and Puck, this issue).

It is important to acknowledge that much of the analysis built on the original I - NR framework, including our extension above, emphasizes the economic costs and benefits accruing to manufacturing and R&D activities, whereas these activities represent only a portion (albeit an important one) of the entire value chain. Nevertheless, the arguments can be extended to other value chain functions, and even to individual tasks, each of which is subject to its own I - NR tensions (Bartlett and Ghoshal, 1989: 97), as well as to more subtle managerial dimensions. For example, just like manufacturing and R&D, marketing also faces competing goals as it needs to weigh the importance of coordinating global brands against the importance of being sensitive to cultural differences (Takeuchi and Porter, 1986). Regional brands may provide a balance between these two goals given that cultural similarity is larger within regions than across them. In procurement, the choice is not simply one between orchestrating a global supplier network and letting each national unit choose its own local suppliers. Instead, regional supply chains may provide sufficient critical mass to enhance bargaining power, while still economizing on the transportation and coordination costs of managing a geographically dispersed procurement network. Similar tensions can be identified in human resource management (Hannon et al., 1995), knowledge management (Asmussen et al., 2013), network embeddedness (Meyer et al., 2011), and so forth—and in each case, a similar argument for the regional level can be made.

Finally, it is worth linking the I - NR discussion to the RBV component of internalization theory as it applies to regional strategy. The tensions we described between economies of scale and adaptation in the present section—and the role of the region in breaking up these tensions—can easily be given an interpretation in terms of new, requisite resource development. On the one hand, as explained by Rugman and Verbeke (1992), a successful ‘global’ strategy necessarily relies on a firm possessing non-location bound FSAs, whereby economies of scale

and scope derive from these non-location bound FSAs that “can be transferred abroad at low marginal cost and used effectively in foreign operations” (Rugman and Verbeke, 1992, p. 765). This suggests that such FSAs are subject to powerful ‘develop once, deploy everywhere’ economies, that may be very important in the case of high integration pressures in industry. Such pressures will be strong if, for example, substantial investments in R&D or marketing are necessary to develop and sustain these FSAs. On the other hand, the ‘multinational’ approach arises when “specific local customer needs and market conditions, as well as government regulation, provide incentives to firms to develop [location-bound FSAs]” (Rugman and Verbeke, 1992, p. 765). The presence of such incentives reflects the firm’s non-location bound FSAs being insufficient, or at least requiring significant linking investments in host markets before they can be leveraged. The need for such investments in location-bound FSAs will be larger in industries where local responsiveness pressures are high. As we have argued in this paper, the regional strategy can be incorporated as a third strategy in which the firm develops FSAs that are neither completely non-location bound in a global sense, nor completely location-bound in a national sense, but ‘region-bound’ as shown in the middle row of [Figure 1](#).

CONCLUSION

This paper has outlined the intellectual foundations of the past and present research in international strategy that has added a regional, geographic dimension to the conventional local (or national) - global dichotomy. This additional dimension has important implications, since it suggests that entrepreneurial opportunities may be available at this intermediate level, and that effective MNE strategy—and effective theorizing about such strategy—may therefore also need to include a regional component. Two important, managerially oriented axes for future research

were identified: (1) explaining the absence of—or boundaries to—global market diversification by most firms, including the dangers of ‘overextending’; and (2) analyzing the organizational elements introduced by firms with a footprint beyond their home region, but taking into account that this footprint and the related organizational arrangements may be vastly different for each value chain activity. In the context of the second point, we have also revisited the classic integration – national responsiveness framework and have assessed the implications for strategy and organization of adding a regional component to the analysis.

It is clear to the authors of this paper that the ‘regional strategy’ agenda is here to stay. This agenda provides rich avenues for advanced research in terms of both usage of sophisticated methodologies and conceptual innovation in a field of inquiry where distance parameters suddenly become much more than simple, continuous variables when the impact of regions is recognized. For example, both insiders and outsiders can be affected very differently by regional integration plans at the macro-level: exploring the processes through which firms adapt their strategies via new resource recombination will allow substantive extensions of internalization theory. Such approach will also allow augmenting the theoretical building blocks of this theory, with its joint foundations in resource based view (RBV) thinking and transaction cost economics (TCE).

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Figure 1: Geographic Locus of International Business Opportunities and Reach of the MNE's extant FSAs.

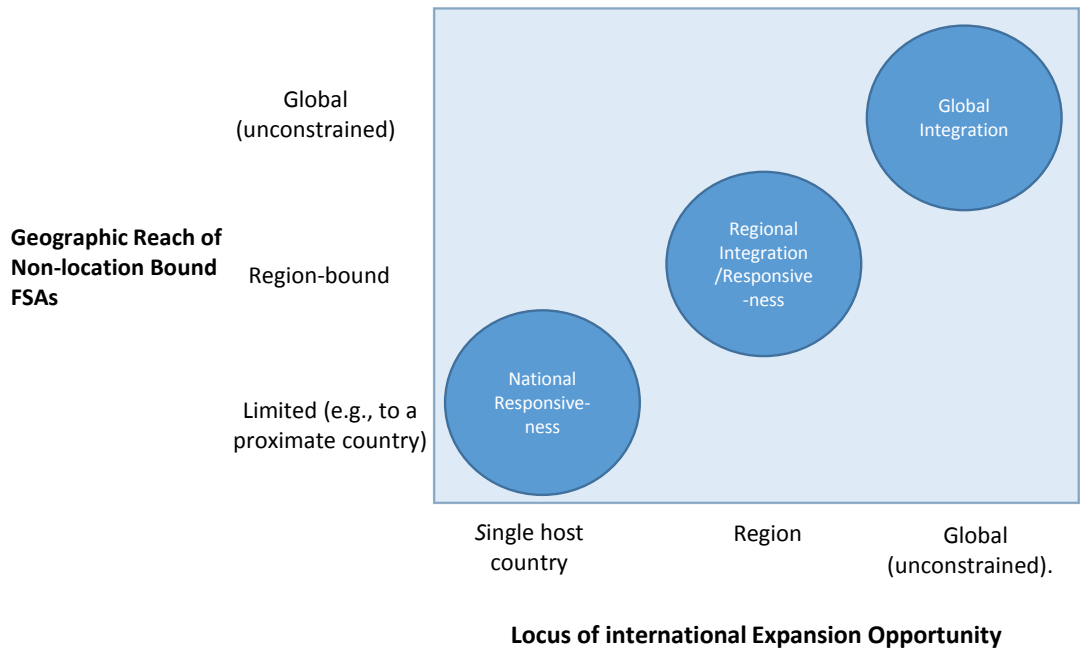


Figure 2: The Classic Integration-Responsiveness Framework

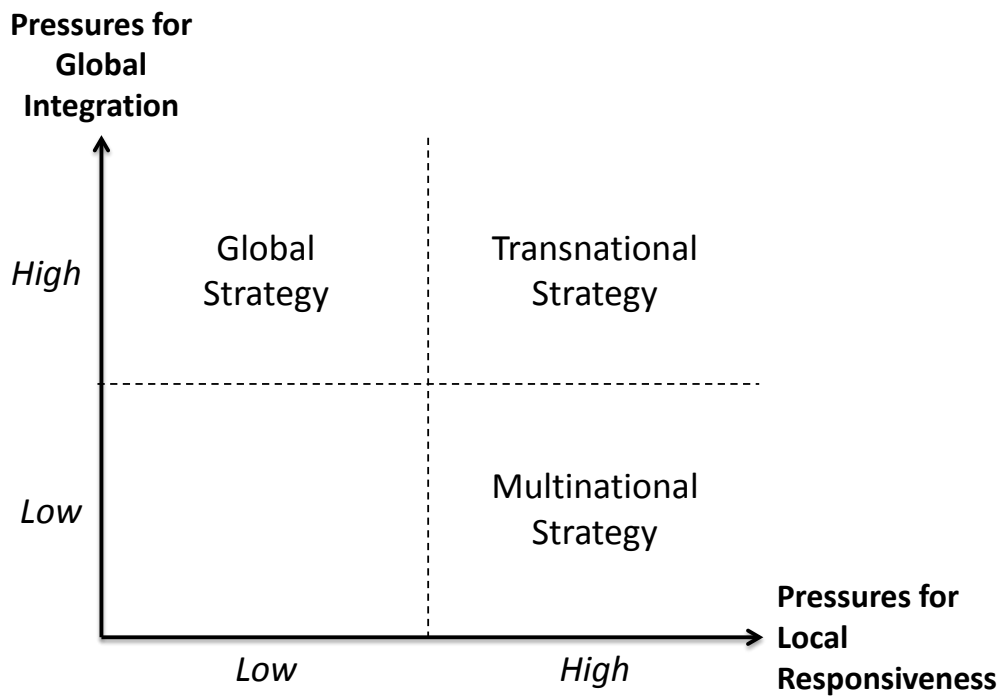


Figure 3: Economies of Scale (EOS) and Minimum Efficient Scale (MES)

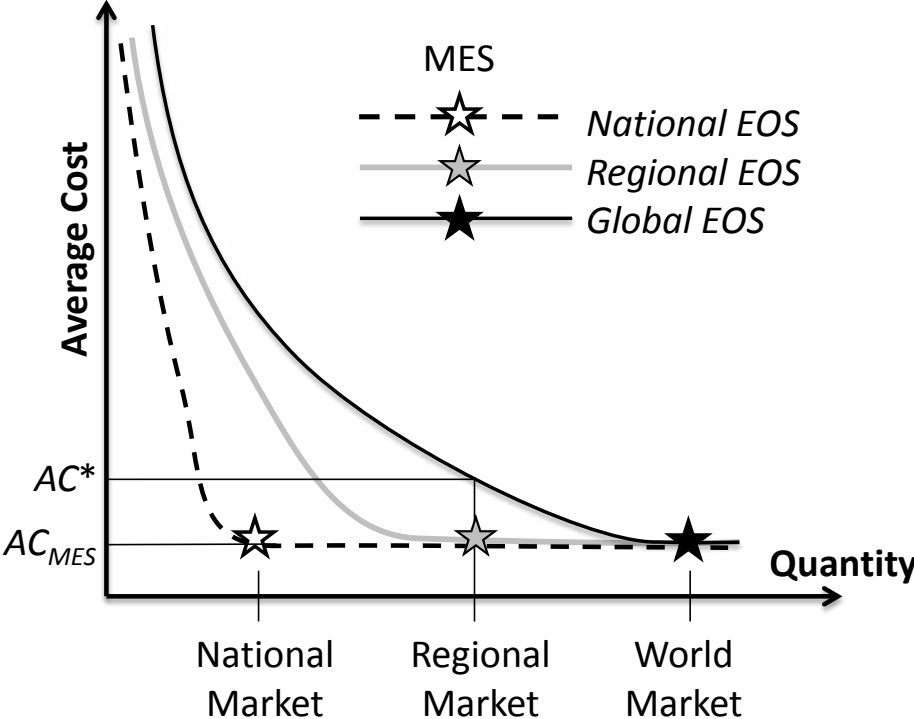


Figure 4: An Extended Integration-Responsiveness Framework



NOTES

¹ Bounded rationality or *BRat* refers to ‘scarcity of mind’, i.e., to individuals’, in this case managers’, limited access to information and to their limited information processing capacity. Bounded reliability or *BRel* refers to ‘scarcity of effort to make good on open-ended promises’. Such limited effort may result from strong-form self-interest, but also from benevolent preference reversal and identity-based discordance (Kano and Verbeke, 2015). *BRat* and *Brel* problems are exacerbated by the various dimensions of ‘distance’, as experienced by MNE managers operating across borders.

² A global firm was defined as having less than 50% of sales in its home region, and at least 20% in each of the two other triad regions. The triad regions considered were the European Union, North America (including Canada, the United States and Mexico), and Asia. Rugman and Verbeke (2004) focused on these three regions because they were the home base of most large MNEs in the world, and the locus of most technological innovations across industries. Subsequent work, focused on the distribution of MNE assets, adopted the same thresholds. A more correct approach would obviously be to calculate the extent to which firm-level market shares in relevant industries in each region (as a cluster of countries) would correspond with – or deviate from – the macro-level market share of those regions in the worldwide sales and asset distribution in these industries. Asmussen (2009) provided metrics based on this logic.

³ Arguably, the field of international business can be defined by its preoccupation with managing across national boundaries. However, if other boundaries than national ones become relevant to management, and where is a need to distinguish between boundaries *within* and across *regions*, this could affect the substance of many questions that international business scholars attempt to address.

⁴ This perspective does not diminish the importance of production costs, which are critical when determining both the scale and location of production operations, but production costs alone typically do not determine the choice of governance mode, such as the choice between a wholly owned subsidiary and a licensing agreement.

⁵ Here, two comments should be made. *First*, Ghoshal (1987) in his now classical article proposing an organizing framework for global strategy, conflated benefits from exploiting national differences with benefits of national responsiveness. The former require non-location bound FSAs, whereas the latter require location-bound ones, see Rugman and Verbeke (1992, footnote 2). *Second*, Ghemawat (2007) later relabeled these mainstream international strategy concepts as aggregation (referring to strategies aimed at reaping economies of scale and scope), arbitrage (referring to strategies aimed at benefits of exploiting national differences) and adaptation (referring to strategies aimed at benefits of national responsiveness).

⁶ Rugman and Verbeke (2007: 203) strongly cautioned against the construction of regions resulting from academic modeling, because: “sophisticated regional classifications are an academic artifact, intellectually appealing but relatively far removed from the practice of international corporate strategy and geo-political reality”. Flores et al. (2013) provide an

overview of alternative regional classification schemes.

⁷ Here, the question could be raised as to the potential benefits of fine-tuning global, i.e., geographically unconstrained FSAs so that they would become region-bound, i.e., geographically constrained. The answer is that the terms ‘global’ and ‘region-bound’ FSAs both describe a capacity for profitable growth vis-à-vis relevant rivals, but do not specify the relative strength of this capacity. Here, resources bundles with a somewhat weaker capacity to establish a profitable global footprint are recombined with resources accessible in the region so as to establish a stronger capacity for profitable growth in that particular region.

⁸ As to the role of product diversification, this is supposed to moderate negatively the positive M - P linkage associated with home region diversification. In contrast, higher product diversification could potentially improve the otherwise negative M - P linkage in case of inter-regional diversification. Here, assumed access by the MNE’s many product areas (especially if unrelated) to valuable external knowledge in distant locations and the subsequent transfer thereof inside the MNE network, could increase productivity. The question arises, however, whether the combination of high inter-regional diversification and product diversification will not amplify further MNE governance complexity.

⁹ Firms may still seek markets outside of their home region, but typically do so with much less success than inside their home region. Asmussen (2009) estimated that it was three times as difficult to penetrate global markets as compared to home regional ones. Asmussen and Goerzen (2013) also showed that retailers were much less dispersed across regions than other types of firms.

¹⁰ The framework discussed in earlier sections, with non-location-bound FSAs and location-bound ones represents an internalization theory (joint TCE/RBV) interpretation of the integration – national responsiveness approach for analyzing MNE choices of strategy and structure (Rugman and Verbeke, 1992; Verbeke, 2013).

¹¹ Alternatively, MNEs could also pursue an ‘international strategy’, whereby replicas of home country operations are set up abroad, thereby leading mainly to economies of scope. Bartlett & Ghoshal (1989) placed such a strategy in the ‘low-low’ quadrant. However, most other authors writing on I – NR strategy challenges ignore this possibility, with both Prahalad and Doz (1987), Bartlett (1986), and subsequent empirical work (Roth and Morrison, 1990) focusing on the three strategies shown in Figure 2. We will, therefore, not discuss this strategy in the subsequent analysis.

¹² Our argumentation in this section is largely intuitive and based on simple, stylized facts. However, an underlying formal model of these trade-offs, describing the boundary conditions of the regional strategy, is available from the authors upon request.