4. Aggregation Strategies

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The previous section dealt the strategy of adaptation, whereby companies adjust to the differences they face operating internationally. This section focuses on a second strategy, aggregation, to overcome differences. Aggregation involves using various grouping devices to create greater economies of scale or scope than country-by-country adaptation allows. The key idea is to find ways to group things so that within-group differences are minimal compared to differences between groups, facilitating the pursuit of cross-border scale or scope economies within groups.

Just as there were many adaptation levers and sublevers, there are many possible bases of aggregation. But in the context of international strategy, an obvious focus is provided by approaches to aggregation that cut across national boundaries and, in particular, ones that operate at the regional (continental) level, i.e., at a level between the individual countries emphasized by adaptation strategies and the whole world.

Regions are of particular interest because of the extent to which international economic activity is regionalized. At the aggregate level, more than one-half of international trade and of foreign direct investment appear to take place within continental regions. Company-level data point in the same direction. Section 2 highlighted the propensity of U.S. companies’ foreign affiliates to cluster in Canada. And even the largest multinationals still exhibit significant home-region bias. Analysis by Alan Rugman and Alain Verbeke shows that of the 366 companies in the Fortune Global 500 for which such data were available, 88 percent derived at least 50 percent of their sales in 2001 from their home regions – with the share of sales in the home region averaging 80 percent for this subgroup. In contrast, just 2 percent of the sample – or nine companies – had sales of at least 20 percent in each of the “triad” regions of North America, Europe, and Asia.

This section will therefore dig deep into a regional approach to aggregation and the multiple subapproaches it subsumes before briefly discussing other bases of aggregation.

Regional Strategy Archetypes

To get a sense of the variety of regional strategies and why they aren’t just watered-down versions of (standardized) global strategies, consider a company that is a global heavyweight that nonetheless emphasizes regionalization as one of the cornerstones of its strategy: Toyota. Toyota’s rapid build-up of manufacturing facilities around the world admittedly led to some significant problems including major product recalls, and financial performance had, as of mid-2010, yet to recover significantly from the recessionary doldrums of 2008-9. However, Toyota is judged to be on track to recover: its equity market value in mid-2010 was roughly three times Ford or Volkswagen’s (its two largest competitors after bankrupt General Motors).
This global heavyweight has, in fact, overlaid a succession of regional strategies on its basic competitive strategy built around the Toyota production system. For its first 50 years, it followed a strategy of *regional focus*: it had essentially one production base, in Japan. But in the 1980s, it started to build more of a *regional portfolio* by making its first significant foreign investments in a second major region, in North America. In the 1990s, Toyota began to create *regional hubs* that were meant to make regions more freestanding and less dependent on Japan by putting in regional design centers and allowing, for the first time, production of a limited number of locally exclusive models.

The 1990s was also roughly when a series of strategic initiatives aimed at achieving more coordination across the regional building blocks—*interregional* rather than *intraregional* strategies—began. Toyota moved towards more (*inter*)regional platforms by promoting “global cars” with more commonality across regions while consolidating the number of major product platforms. It began awarding some plants or regions (*inter*)regional mandates for scale-sensitive parts and systems such as engines and transmissions. And it envisages an even more extensive (*inter*)regional network going forward—but one still overlaid on the regions as the fundamental building blocks (because of concerns about protectionism as well as fundamental differences in gas prices across regions).

Exhibit 1 summarizes the six regional strategy archetypes cited above. Note that the focus of boxes 1 through 3 is intraregional, in a sense, while that of boxes 4 through 6 is interregional. The boxes represent progressively more complex—and less common—approaches to dealing with regional boundaries. However, it is worth noting that there is no natural order of progression through these regional strategy archetypes. Different regional strategies make sense for different businesses. The rest of this section discusses the objectives and limitations of each strategy.

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**Figure 1: Regional Strategies**

<table>
<thead>
<tr>
<th>1. Regional Focus</th>
<th>2. Regional Portfolio</th>
<th>3. Regional Hubs</th>
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<tr>
<td><img src="image" alt="Home Scale/Position" /></td>
<td><img src="image" alt="Growth Option, Risk Reduction" /></td>
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<td><img src="image" alt="Sharing across Regions" /></td>
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<td><img src="image" alt="Integration across Regions" /></td>
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Increasing Complexity of Managerial Challenges: Regional Development, Support, Control and Coordination

Decreasing Incidence

Note: The dots can be interpreted as distinct product types; $R_1$ and $R_2$ represent two regions.
1. Regional or Home Focus

While focus was already discussed in Section 3 in the context of managing adaptation, focus along geographic or regional dimensions is worth reemphasizing because virtually all companies start off in this box, except for the very few that are “born global” (often in high-technology areas). This is also the box in which nearly 90 percent of the Fortune Global 500 still reside, in terms of the revenue based definition introduced above. Focusing on selling to one region is favored in a number of circumstances, including:

- A particularly profitable regional or home market (although this is likely to attract entrants from other regions)
- A need for deep local knowledge that reduces efficient breadth
- A high sensitivity to regional free-trade arrangements and regional preferences
- Other factors that effectively collapse the distance within regions relative to the distance between them (e.g. regional monetary unions or energy grids)

Other companies should be placed in this box based on their production footprints. Thus, in the highly globalized memory chip (DRAM) business, Samsung sells worldwide but considers the co-location of most R&D and production around one main site in South Korea as a key competitive advantage. Given how low transport costs are relative to product value, geographic concentration – which permits rapid iteration across R&D and production – dominates dispersion. More generally, a regional or home focus for production activities is attractive when global scale economies are strong enough to permit centralization of at least some activities in one region or location, or when key economies of scale operate at the regional, rather than local or global, level.

Many of the risks associated with regional or home focus relate to the erosion of the conditions underpinning its viability relative to more globally standardized strategies. Also, regional focusers can run out of room to grow or fail to hedge risk adequately, motivating broader expansion efforts.

2. Regional Portfolio

Box 2 – the regional portfolio – comprises strategies that involve more extensive operation outside a single region. Particular stimuli to move in this direction include faster growth in nonhome regions, significant home positions that generate substantial free cash flow, local investment requirements to access foreign markets, and the opportunity to “average out” shocks, cycles, and so forth, across regions.
Regional portfolio strategies may migrate some resource allocation and monitoring roles from corporate headquarters to regional entities. Apart from that, however, they offer little room for regional considerations to influence what happens on the ground locally.

3. Regional Hubs

A more active alternative for adding value at the regional level was originally articulated by Kenichi Ohmae in his notion of “triad” strategy. This involves building regional bases or hubs that provide a variety of shared resources or services to the local (country) operations. The logic is that these hubs may – because of lumpiness, or increasing returns to scale, or externalities – be hard for any one country to justify, but still be worth investing in from a cross-border perspective. Although one or a few locations often provide such shared resources and services, the hub may sometimes be a virtual one.

Regional hub strategies in their purest form – that is, those focused solely on regional position – represent a structured multiregional version of the regionally focused strategies discussed in box 1 of the figure. Therefore, some of the same conditions that favor a regional focus also favor regional hubs. The difference is that with more than one region, considerations of interregional heterogeneity also come into play. The more that regions differ in their requirements, the weaker the case for sharing across multiple, regionally focused entities within a company.

A regional headquarters (RHQ) can be seen as a minimalist version of a regional hub. The impact of an RHQ is typically limited, however, by a focus on support functions, with limited links to operating activities. Phillipe Lasserre has developed a list of key RHQ functions that can help broaden the possibilities companies may wish to consider: scouting (business development), strategic stimulation (helping organizational subunits understand and deal with the regional environment), signaling commitment to a region (to internal and external audiences), coordination (ensuring the exploitation of synergies and the pursuit of consistent policies across the region), and pooling resources (to take advantage of regional scale economies).

4. Regional Platforms

Regional hubs, as we have seen, spread fixed costs across the countries within a region. Regional platforms, by contrast, spread fixed costs across regions – and could, therefore, also be described as “interregional platforms.” Platforming is typically emphasized for back-end activities that deliver scale and scope benefits if coordinated across regions. Thus, major automakers attempt to reduce the number of basic platforms they offer worldwide to achieve greater economies of scale in terms of design costs, engineering, administration, procurement, and operations. The goal is not to reduce the amount of product variety on offer, but instead to deliver variety more cost effectively by building local customization atop common platforms explicitly engineered for such adaptability.

The principal risk inherent in platforming strategies is that companies may take standardization too far, at the expense of the variation required for the local marketplace.
A tendency toward centralization of key decisions about interregional coordination at corporate headquarters reinforces the risk of excessive standardization across regions.

5. **Regional Mandates**

Regional mandates can also be described as interregional mandates, because they involve awarding broader mandates to certain regions to supply particular products or to perform particular organizational roles in order to tap economies of specialization as well as scale. Suzuki, for instance, sources its small cars from its Indian subsidiary, Maruti Suzuki. And a host of global companies are in the process of broadening the mandates of their production operations in China.

(Inter)regional mandates also show up in areas that go beyond product development and production. Thus, global consulting, engineering, financial services, and other service businesses often feature centers of excellence – repositories of particular knowledge and skills that are charged with making them available to the rest of the firm.

Again, there are several risks associated with assigning broad geographic mandates to particular locations. First, they can supply cover for local, national, or regional interests to unduly influence, or even hijack, a firm’s global strategy. Second, broad mandates are not well suited to picking up on variations in local, national, or regional conditions, although overlaying other approaches such as platforming can be of some help here. And finally, carrying the degree of specialization to extremes can create inflexibility and lack of redundancy. In a volatile world, these are significant concerns.

6. **Regional Networks**

To achieve complementarities across different regions, while avoiding excessive inflexibility, regional networks rely on integration as well as specialization through division of labor among resources located in different regions. Although academics have discussed networking extensively, most companies merely aspire to such integration.

*From Regionalization to Aggregation*

Thinking through a range of regional strategies – both their attractions and their limitations – is a useful way of analyzing aggregation possibilities. But aggregation offers a much broader canvas for companies thinking about how to tap greater economies of scale across national borders. To begin increasing the range of options, consider different levels at which geographic regions can be defined – not just continental but also subcontinental, national, intranational, or local. Thus, the recent proposal that (highly internationalized) companies organize regional “hub” operations in twenty “gateway” cities countries, ten in industrialized countries and ten in developing countries, each serving five to ten countries, may be considered as a variant of regional aggregation at the subcontinental level. Assessing the level at which scale is most tightly tied to profitability is often a helpful guide to appropriate geographic scaling.
In addition to rescaling geography, one can be even more creative and focus on distance – and regions – along nongeographic dimensions: cultural, administrative or political, and economic. Examples of aggregation along a cultural dimension include companies that group together countries by common language (e.g. Spain and Latin American countries). In the administrative realm, the defense contractor Raytheon created a “Commonwealth marketing group” based on the finding that British Commonwealth countries shared similar procurement procedures and practices. Companies that group together developed versus emerging markets aggregate on an economic dimension. And while the CAGE framework naturally focuses attention on countries (or other geographic units) as the basis for grouping, there are also other, noncountry, bases of cross-border aggregation that companies have implemented: channels, client industries, global accounts and, for multibusiness firms, global business units.

Conclusion

Aggregation represents a powerful way tapping more economies of scale/scope than country-by-country adaptation strategies allow. And each of the bases of aggregation, of which geography is just one possibility, offers multiple possibilities for crafting strategies intermediate to the local and global levels by grouping things so that the differences within groups are smaller than the differences across groups.

That said, aggregation is not a panacea, for several reasons. First, aggregation always carries the risk of creating silos that disrupt organizational functioning. Second, aggregation also tends to increase organizational complexity, given all the linking mechanisms that it necessitates – especially when aggregation is attempted along multiple dimensions. Third, since it is usually impossible to implement all imaginable forms of aggregation, it is important to select among them carefully. The CAGE Distance framework and ADDING Value scorecard are useful tools for identifying and evaluating potential bases for aggregation. And fourth, frequent shuffling of bases of aggregation, while not unknown in the business world, is almost invariably a recipe for disaster since it tends to take years to make a basis of aggregation work. So, aggregation strategies must be chosen with an eye to long term sustainability.

1 For a more extended treatment of this material, see Chapter 5 of Pankaj Ghemawat, Redefining Global Strategy (Harvard Business School Press, 2007) and the other references listed therein. Regional strategies are also elaborated further in in Pankaj Ghemawat, “Regional Strategies for Global Leadership,” Harvard Business Review, December 2005.


3 These proportions are sensitive to the definitions employed and cutoffs used; in addition, it does appear that the percentage of the very largest firms that are focused on their home-regions has dropped over time (in contrast to the apparently increasing regionalization of world trade). See Thomas Osegowitsch and André Sammartino, “Reassessing (Home-)Regionalisation,” Journal of International Business Studies (2008) 39, 184–196.