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The Size and Composition of Corporate Headquarters in Multinational Companies: Empirical Evidence

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ABSTRACT

Based on a six country survey of nearly 250 multinationals (MNCs), this paper is the first empirical analysis to describe the size and composition of MNC headquarters and to account for differences among them.

Findings are that: MNC corporate headquarters are more involved in "obligatory" and value creating and control functions than in operational activities; there are no systematic differences in the determinants of the size and composition of corporate headquarters between MNCs and purely domestic companies; as the geographic scope of an MNC increases two offsetting phenomena occur — headquarters decrease their influence over operational units which ceteris paribus reduces the size of headquarters, but the relative size of obligatory functions at headquarters increases with increased country heterogeneity. The net effect is that the size of corporate headquarters expands as MNC geographic scope increases. The notion of "administrative heritage" is validated as MNCs from different countries have substantially different corporate headquarters — US headquarters are large (255 median staff for a 20,000 FTE MNC) and European headquarters smaller (124).

Implications are drawn that countries will lose activities if domestic firms are acquired by foreign MNCs, and that MNCs need to allow more subsidiary autonomy as their geographic scope increases.

1. Introduction and motivation

Multinational corporations (MNCs) are a ubiquitous feature of the modern economy, accounting for about one quarter of global output and one third of international trade (Jensen, 2006). Their importance to economic activity increases as the global economy becomes increasingly integrated, and, notwithstanding the interruption caused by the recent financial crisis and recession, that role is likely to continue to expand (World Bank, 2010) since there remains substantial deviation from perfectly integrated global markets (Ghemawat, 2011).

Given this importance of the multinational corporation there has been much research on its role and functioning as an institution (Bartlett and Ghoshal, 1989; Birkinshaw et al., 2003; Rugman and Verbeke, 2005). However, one aspect of that entity — the role headquarters play within the MNC — although it has seen interest from various disciplines, has been understudied. While corporate headquarters in general, but not specifically in MNCs, have been the subject of research (Collis et al., 2007, 2009; Markides, 2002), and while attention in the last decade has focused on the roles played by country subsidiaries within an MNC (Birkinshaw and Hood, 1998; Holm and Pedersen, 2000), less attention has been paid to the specific role that MNC headquarters perform. This paper represents an attempt to remedy that dearth of research by explicitly examining the size and composition of headquarters in multinational corporations.

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At the macroeconomic level, decisions as to what activities occur at the headquarters location in the home country affect the activities that take place in subsidiaries elsewhere. Taken to the extreme, this raises the fear that unless corporate headquarters are based in a country, high value added headquarters jobs will leave the country, so that, as was said of Australia, it will become merely a “branch office economy” (Garnaut, 2002). This concern over the effect of nationality of ownership on jobs (Reich, 1990) has led to government objections to takeovers of domestic companies (e.g., Canada's recent reaction to a bid for Potash, Erman, 2010). While prior studies have found limited substitution between home country and foreign activities — for example, there was shown to be little or no impact on R&D in Sweden after the acquisition of domestic firms by foreign MNCs (Bandick et al., 2010) — understanding which activities take place in MNC headquarters should offer additional insight into this important policy issue.

MNC executives have struggled to define an appropriate role for headquarters to effectively create value from international activities. The frequent large scale reorganizations and rightsizing (in either direction) of an MNC's headquarters illustrate how unsure many are as to the optimal structure and influence of that entity (Bartlett, 1983). The classic recent example is Coca Cola Enterprises that has gone from slashing Atlanta headquarters by 6000 employees in 2000 in order to push decision-making into the countries, to reinstating people and tasks at Atlanta under a new CEO after 2004 (Ghemawat, 2007). Similarly, a recent turnaround at Kraft has been attributed to the decision to delegate substantial authority from corporate headquarters to country management (Rosenfeld, 2009).

Strategists, organizational design, and international business scholars have therefore sought to develop prescriptions for the optimal allocation of tasks between headquarters and country subsidiaries (Bartlett and Ghoshal, 1989; Forsgren et al., 2005; Galbraith, 2000).[1] For them, the challenge is to balance the tensions inherent in operating internationally — achieving global efficiency and dynamic arbitrage, while maintaining the flexibility to adapt to local market requirements (Bartlett and Ghoshal, 1989; Ghemawat, 2007). This has led to specific recommendations concerning headquarters design that seek to balance the requirements of centralization with decentralization (Bartlett and Ghoshal, 1989); that illustrate how headquarters' relations with subsidiaries depend on the international strategy and underlying nature of the resource that underpins the competitive advantage of the MNC (Calori et al., 2000; Porter, 1986; Rugman and Verbeke, 2001); and that show the effect of differences in the institutional environments of countries in which the MNC operates on the allocation of activities to those subsidiaries, and therefore on the responsibilities of headquarters[2] (Birkinshaw et al., 1998; Paterson and Brock, 2002).

While this work is valuable, there has been a dearth of empirical research that examines what actually goes on at the headquarters of MNCs. This paper seeks to remedy that deficiency by analyzing the size, composition, and determinants of activities at the corporate headquarters of a sample of 244 MNCs based in the US, UK, Germany, France, Netherlands, and Chile. Its aim is to answer basic questions concerning, first, a description of the type and size of activities that are undertaken at headquarters and, second, what determines those choices, including whether they differ from purely domestic corporations; how they change as the geographic scope of the MNC expands; and whether there are significant differences among countries. Its findings provide suggestions for policymakers confronting the takeover of an important domestic firm by a foreign multinational, and MNC executives struggling with the design of corporate headquarters and its relationship with foreign subsidiaries.

2. Related literature and hypotheses

There are two streams of literature that provide theoretical insight into the role of headquarters in the MNC. The first is strategy research on the role of corporate headquarters in diversified or multi-business corporations (Collis et al., 2007; Foss, 1997; Markides, 2002). This covers a broader set of firms than simply MNCs but has direct applicability to the more specific phenomenon of headquarters in companies that operate across borders since both address multi-market activity.[3] The second is the international business literature on the design of the headquarters–subsidiary relationship that specifically addresses MNCs but which has most recently focused on the subsidiaries, rather than the headquarter's role (Birkinshaw and Hood, 1998).

2.1. Corporate headquarters

Research on corporate headquarters began with Chandler's seminal work on the emergence of the M-form corporation (Chandler, 1962). He identified the corporate headquarters, or “general office”, separate from the operating units as the distinguishing feature of the M-form corporation, and first classified the two unique functions of that entity as being “coordinate, appraise and plan goals and policies” and “allocate resources”. In doing this he began to address the fundamental question for multi-business entities of how to add value beyond that which the lines of business could generate by themselves or through market contracts.

On revisiting the issue, and aware of advances in agency theory (Jensen and Meckling, 1976), Chandler later reclassified the roles of headquarters into “entrepreneurial” (value creating), and “administrative” (loss preventive) (Chandler, 1991). More recent observers have taken a more nuanced approach by distinguishing more roles for the corporate office and arguing that the determinants of the size of each will be different (Foss, 1997; Markides, 2002). In particular, Collis et al. classified the set of activities performed at corporate headquarters to distinguish the “obligatory functions” required of any corporate entity (tax and

[1] The intermediate role of regional headquarters has recently also been a focus of study (Enright, 2005).
[2] Recently the impact of institutional factors on the location of headquarters itself has been investigated (Benito et al., 2011; Laamanen et al., 2012).
[3] Both multibusiness and multinational strategy address issues of value creation, and the design of organizations that control delegated decision-making and coordinate activities across multiple markets. Of course, a corporation can be both multi-business and multinational — as are most companies in our sample.