

Sculpting the New Style of Global Strategic Management:

Middle-Sized Companies Facing Global Dilemma

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1. INTRODUCTION

During the 1980's the world witnessed a rapid globalization of Japanese companies. In contrast to the boundaries limited by the traditional internationalization of business, which was mainly export-orientated, companies started to adapt a new strategy represented by the shift of sales offices, production facilities, and R&D facilities to overseas. By the late 1980's Japanese companies, backed by their booming domestic operations, had firmly established themselves overseas. In regards to most of the small manufacturers of parts, their overseas expansion was in response to large scale expansions by large assemblers. The result was a separation of sales and production, in which the market was in developed countries and the production were in developing countries.

However in the 1990's the world saw the rapid economic growth of Asian countries, which until then had only been regarded as the low cost production region. In addition, the strength of the Japanese companies were deteriorated by the diminishing Japanese economy, and at the same time European and the U.S. companies, which were in the shadow of the Japanese companies during the 1980's, started to gain momentum once again. On top of that in midst of worldwide trend of deregulation of industries, even Japan who had been more or less closed to the foreign firms, started to open its market. The arrival of the "global competition"

demanded changes to Japanese companies' traditional strategy, which had been sneered as the "convoy" system by foreigners for a long time.

Under these circumstances, Japanese companies could not help but change their global strategy, and unless they did so they could not expect to survive the fierce competition in the 21st century. In order to compete evenly against companies all over the world, it became necessary to leave behind the internally developed management style, which had been honored for so long.

This article discusses the strategies the Japanese companies are contemplating and implementing in order to adapt to the changes in the global business environment.

2. LITERATURE REVIEW and RESEARCH FRAMEWORK

The research conducted by Vernon (1966), known as the Product Life Cycle Theory, was the first to go beyond the macro economics' point of view of international economics, and research into internationalization from the point of view of individual companies. Thereafter Hymer (1976) presented the methodology for increasing competitiveness for companies producing overseas. That was followed by Stopford and Wells (1972) who conducted research on multi-national companies' ownership and organizational structures. During the 1970's, theoretical research on internationalization moved beyond the boundaries of international economics and became more orientated towards management and strategy.

As best represented by Dunning's (1980, 1988) research, theoretical research on internationalization during the 1980's focused on what kinds of competitive edges overseas operations are capable of achieving and how they are able to do so. At the same time, attention was paid to the various stages of internationalization and the management systems which directly affect those stages (Henan & Pearlmutter). In the late 1980's there

was a greater significance placed on the company's strategic decisions and the pattern and the process of internationalization. As a result, a further research was conducted about; the relationships and the delegation of responsibilities between the parent and the subsidiary, the management structures, the management systems, and how these elements related to one another (Ghoshal & Berttelet, 1991; 1994).

The trend of these research topics was due to the increased difficulties in fully explaining an internationalization of a company by looking at only the head quarters' (HQ) strategy and management system. In other words, competitive edge was no longer created solely by the HQ, and the role of overseas subsidiaries has become significant in order to create and maintain the competitive edge for the whole company. The fact that a business needs to be looked at from a global point of view began to be realized, and it was also reinforced by experience. For example, it was reported by Bartlett & Ghoshal (1986) that in many cases overseas subsidiaries are significant contributors and leaders for revolutionary company wide projects. Overseas subsidiaries are capable of providing values to other areas within the company (Gupta & Govindarajan, 1994), also capable of gaining authority for production control for a product line of a global scale (Ruth & Morrison, 1992). In fact, research shows that words such as specialized contributors, strategic leaders, or aggressive subsidiaries have been used to describe overseas subsidiaries that significantly contributed to achieving competitive edge for the whole company. On the other hand, for those overseas subsidiaries that fall short of making contributions as mentioned above, words such as implementers and branch factories are used.

Birkinshaw et al (1998) defines various theoretical researches on global company management into three categories. The first is the determinism. Multi-national companies recognize the different environmental factors that surround them, and the duties they must

accomplish. In most cases they see their overseas subsidiaries only as one of the local environmental factors (Ghoshal & Nohria, 1989; Westney, 1994). In instances where the overseas subsidiaries are strategically important (Bartlett & Ghoshal, 1986), or where the influence of the local competitors, suppliers, and customers are significant (Porter, 1990), the subsidiary's role is viewed as more important accordingly. Concepts such as adapting to the local environment, and global consolidation (Jarillo & Martinez, 1990) are interpreted within the paradigm of determinism.

The second view is the HQ assignment theory. Under this theory the HQ has the authority to decide the strategic responsibilities for the whole company, and clearly defines them to all of the business units. The HQ must efficiently assign these responsibilities to the subsidiaries in a way that the overall strategic goals are best achieved. This mechanism relies significantly on networks of as control and adjustment, and by directing the activities of the subsidiary managers the role of the subsidiary is decided (Birkinshaw & Morrison, 1996; Gupta & Govindarajan, 1994; Roth & Morrison, 1992). It has also been pointed out that under this theory, subsidiary's roles are adjusted according to the market demand and growth.

The third point of view is choice by the subsidiary. The subsidiary manager is delegated the authority to decide the role of the subsidiary for itself (Child, 1972). Under this view, the overseas subsidiary has a better understanding about the facts and the potentials of the local market than the head office. Therefore the subsidiary is in the best position to decide what roles and responsibilities it must take on. White & Poynter (1984) and D'Cruz (1986) place significance on; resources and skills specific to the subsidiary, expectation towards the subsidiary, and employees' initiative and efforts as the determining factors for the role and the responsibility of the subsidiary.

All of the above three perspectives are convincing. In order to fully

explain the process of true globalization, it must be approached from; the subsidiary's, the whole company's, the industry's, the country's, and comprehensive point of view.

However, it must be pointed out that many of these researches have been conducted based on the data of large corporations. When the market and the competition expand globally, small businesses that traditionally had been conducting businesses only in the domestic market can not help but adapt a global way of thinking also. If so, are their global strategies similar to those employed by large corporations? If there are differences, what are they? Also, will using the same strategy as the large corporation work for small and middle-sized businesses? There is a need to reevaluate Japanese company's strategies with these questions in mind.

The following section will analyze the strategies of the Japanese companies based on a large volume of data from small and middle-sized businesses, which had been overlooked in past researches. Research questions are:

1. What factors will influence global strategies and management decisions.
2. How to recognize the differences between the various strategic options from management's point of view.
3. What organizational and management systems are being considered for large and small companies, respectively.
4. Under the turbulent business environment, how middle-sized Japanese companies should change their management systems.

3. DATA and METHODS

3-1 Data

In this study, the questionnaires were mailed to 1200 Japanese manufacturing companies and 220 valid responses were received (sample

Table 3-1 : Profiles of the sample

Variables	Categories	Number of Cases
Firm size	under 50 billion yen	86
	50-200	63
	200-	51
	n.a.	20
	total	220
Industry	Food	12
	Textile	10
	Paper	2
	Chemical	27
	Drugs	10
	Rubber	2
	Stone, clay and glass	11
	Steel	5
	Metal except steel	3
	Fabricated metal products	6
	Machinery	28
	Electronic equipment	49
	Transportation equipment	31
	Measuring, analyzing, and controlling instruments	7
	other	16
n.a.	1	
total	220	

response rate was 18.4%.) The survey was conducted in November of 1997 and was supported by the Japan Management Association. The profile of the sample is shown in Table 3-1.

3-2 Methods

The questionnaire consisted of 14 items related to firms' behaviors of strategy, organization and personnel system. Questionnaire items are listed in the left column of Table 3-2. Responses were scored on a 5 or 6 point

scale ; from scale of 1 (“not significant”, “negative” or “very low”) to 5 or 6 (“significant”, “positive” or “very high”).

In order to clarify the globalization of Japanese companies more precisely, we analyzed the database by two basic structural variables; firm size and target market. We categorized firm size into 2 types by the median of consolidated sales of the sample; “large-sized” (not less than 60 billion yen of consolidated sales) and “middle-sized” (not more than 60 billion yen.) Target markets, where firms intend to expand into was divided into 3 categories. They are “Domestic”, “Unfocused” and “Global”. The first group or “Domestic” represents those companies that regard the Japanese domestic market as the most important market for them. “Unfocused” represents those who have no clear distinctions between domestic market and overseas market, and therefore their main target markets are unfocused. Finally, the third group or “Global” represents those companies who develop overseas market more intensively than “Domestic” or “Unfocused” companies

Table 3-2 categorizes responses by firm size and target market. In regards to firm size, almost all category means of large-sized firms are greater than that of middle-sized companies. As a whole, it shows that large-sized firms take more aggressive behaviors than middle-sized firms. On the other hand, there are differences among target market categories where “Global” companies take more aggressive behaviors than “Domestic” or “Unfocused.”

When both firm size and target markets are considered simultaneously, it can be summarized into 6 categories; namely, “large-sized Global”, “large-sized Unfocused”, “large-sized Domestic”, “middle-sized Global”, “middle-sized Unfocused”, “middle-sized Domestic.” Under this condition, two-way ANOVA (Analysis of Variance) tests was conducted to check the significance of the independence and joint effects of firm size and target markets on these 14 items. We will test F values of

Table 3-2 : Comparative profiles of the sample: averages of item scores

	ITEM	Firm size		Target market		
		Middle	Large	Global	Unfocused	Domestic
Strategy	Development of new products	4.55	4.65	4.65	4.64	4.74
	Add values to present products	4.08	4.30	3.89	4.30	4.24
	Reduce production cost	4.64	4.62	4.59	4.64	4.63
	Increase domestic R&D investment	3.69	3.75	3.68	3.80	3.61
Organization	Global strategy led by headquarter (HQ)	3.31	3.52	3.81	3.72	2.57
	Technology/know-how transferred from HQ to subsidiaries	2.89	3.43	3.05	3.44	2.74
	Technology/know-how transferred from subsidiaries to HQ	2.28	2.72	2.46	2.69	2.17
	Extend alliances with overseas firms	3.25	3.63	3.59	3.57	3.09
Personnel System	Global standardization of personnel philosophy	3.18	3.62	3.65	3.43	3.13
	Global standardization of personnel evaluation system	3.00	3.30	3.41	3.15	2.93
	Employment regardless nationalities	3.40	3.73	3.76	3.63	3.28
	Enhance international rotation of personnel	3.33	3.88	3.86	3.73	3.15
	Compensation in accordance with personnel evaluation	4.07	4.02	4.14	4.06	3.96
	Organized personnel training for overseas subsidiaries	3.75	4.17	4.19	4.17	3.39

the model, interaction effect, firm size and target market, respectively.

4. RESULTS

Results of two-way ANOVA are presented in Table 4-1. The effects of firm size and target market on strategy, organization and personnel system will be discussed here.

Table 4-1 : Independent and interaction effects of firm size and target markets on strategy, organization and personnel system:
F values from two-way ANOVA test

ITEM		F values			
		Firm size	Target market	Interaction effect	Model
Strategy	Development of new products	0.512	0.167	2.262	0.960
	Add values to present products	10.171***	8.416*	2.522	4.791***
	Reduce production cost	0.459	0.042	1.137	0.557
	Increase domestic R&D investment	0.245	0.751	3.059*	1.878
Organization	Global strategy led by headquarter (HQ)	0.213	22.464***	0.585	11.826***
	Technology/know-how transferred from HQ to subsidiaries	2.558	4.738***	0.609	4.312***
	Technology/know-how transferred from subsidiaries to HQ	10.285***	4.679***	1.277	6.163***
	Extend alliances with overseas firms	5.923*	1.771	0.330	2.843*
Personnel System	Global standardization of personnel philosophy	5.671*	2.131	0.207	3.231***
	Global standardization of personnel evaluation system	2.768	3.186	0.020	2.596
	Employment regardless nationalities	2.013	4.303*	2.225	4.532***
	Enhance international rotation of personnel	9.225***	10.379***	0.852	10.318***
	Compensation in accordance with personnel evaluation	3.641	1.308	7.684***	3.499***
	Organized personnel training for overseas subsidiaries	6.586***	13.858***	1.194	11.289***

Statistical test : significance level $p < 0.01$ ***, $p < 0.05$ *

4-1 Strategy

There were no statistically significant differences among category means in “development of new products” and “reduce production cost.”

This is because almost all companies similarly regard these strategy as critical factors for creating competitive advantage. On the other hand, in terms of “add values to present products” we found significant effects due to both firm size and market targets on category means (see Figure 4-1.) It was revealed that large-sized companies take more aggressive action than middle-sized companies and that “Domestic” as well as “Unfocused” companies take more aggressive behaviors than “Global” companies. In this analysis, it is very interesting that “middle-sized Global” companies obviously do not intend to add values to their present products. As Japanese “middle-sized Global” companies have only followed the globalization of their customers, or large-sized firms, those companies have not had to add values on their products themselves.

Interaction effects between firm size and target markets were found in “increase domestic R&D investment”, while F value of the model was not statistically significant (see Figure 4-2.) Among “Domestic” or “Unfocused” companies, large-sized firms have regarded domestic R&D

Figure 4-1 : Add values to present products

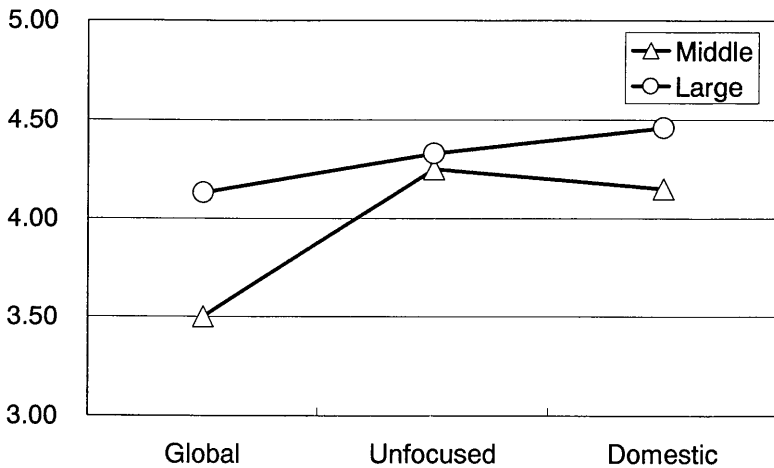
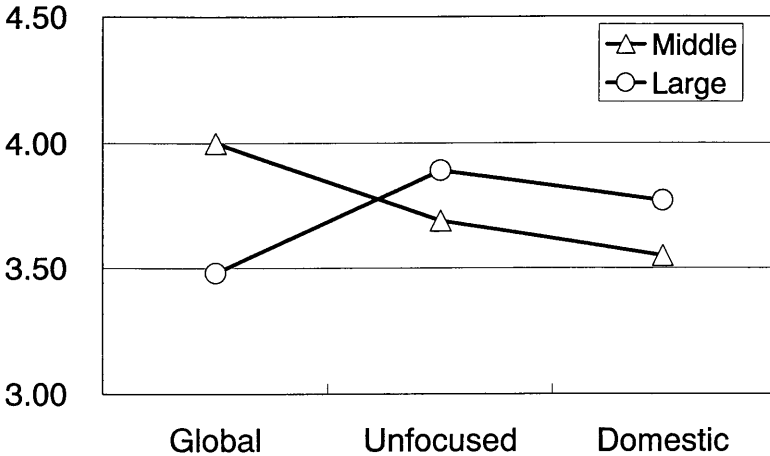


Figure 4-2 : Increase domestic R&D investment



investment as important. On the contrary, among “Global” companies, middle-sized companies invest in domestic R&D more aggressively than large-sized companies.

As far as “middle-sized Global” companies are concerned, methodology for their globalization is increasing R&D investment in Japan. This means creating products only to satisfy their existing customer needs, and simply following global developments of their customers or large-sized Japanese firms. It is a more passive globalization in contrast to that of large-sized firms.

4-2 Organization

In this section, the analysis of the headquarter (HQ) control, technology / know-how transfer and strategic alliances will be discussed.

The effects of firm size and target market on HQ control are revealed in Figure 4-3. Among “Unfocused” or “Domestic” firms, there are significant differences between large-sized and middle-sized, and large-

Figure 4-3 : Global strategy led by HQ

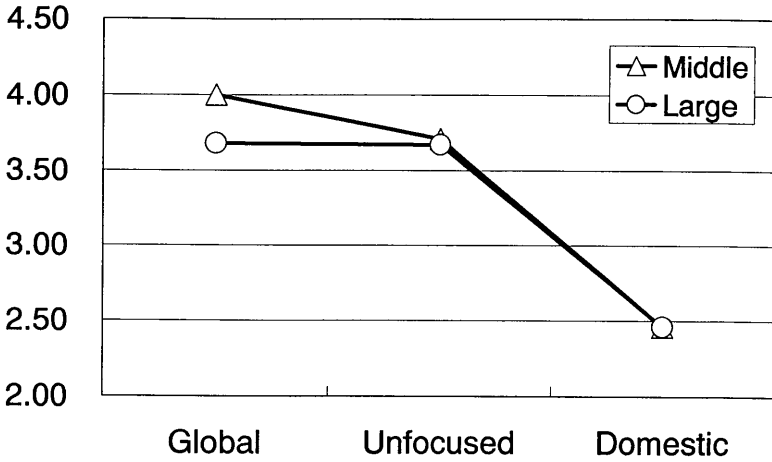
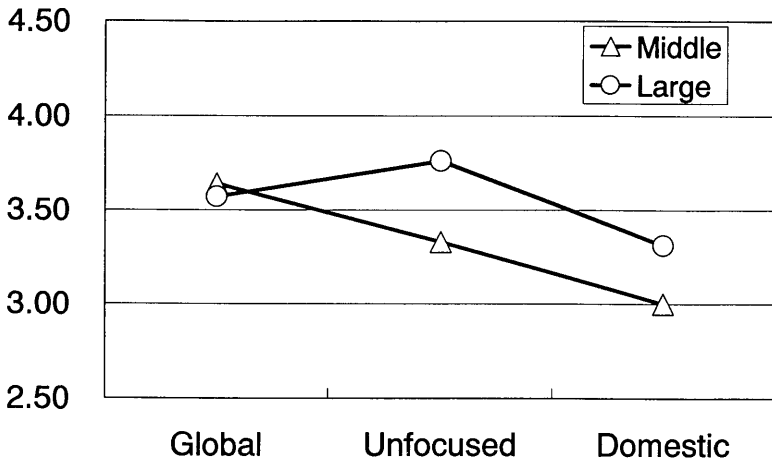


Figure 4-4 : Extend alliances with overseas firms



sized firms have tight HQ control over global strategy. On the contrary, there are no differences between large-sized and middle-sized companies among “Global” companies. Limiting to middle-sized companies, tighter HQ controls were found in “Global” companies than in “Domestic” or “Unfocused” firms.

In terms of technology / know-how transfer, the effect of firm size were significantly greater than that of target market. Both types of transfers; “from headquarter to subsidiaries”, and “from subsidiaries to headquarters” were more evident in large-sized firms than in middle-sized firms. Bartlett and Ghoshal (1989)’s “transnational companies” would be found in such large-sized global companies.

Figure 4-4 shows that ,regardless of firm size, “Global” or “Unfocused” companies developed strategic alliances with overseas companies more intensively than “Domestic” companies. Among “Global” companies, it could be worth mentioning that middle-sized take more aggressive action than large-sized companies, although it isn’t statistical significant.

4-3 Personnel System

We will analyze the database from the view of personnel philosophy and personnel system. The more globalized the business is, the more complex is the human resource management system. Therefore, one methodology for overcoming system complexity is to standardize personnel philosophy and personnel evaluation system. When it comes to global standardization of personnel philosophy, middle-sized companies were more aggressive than large-sized firms, although there is no significant effect of target markets. We can conclude that management based on the Japanese way of thinking is still dominant in middle-sized companies.

On the other hand, the effects of both “organized personnel training

Figure 4-5 : Organized personnel training for overseas subsidiaries

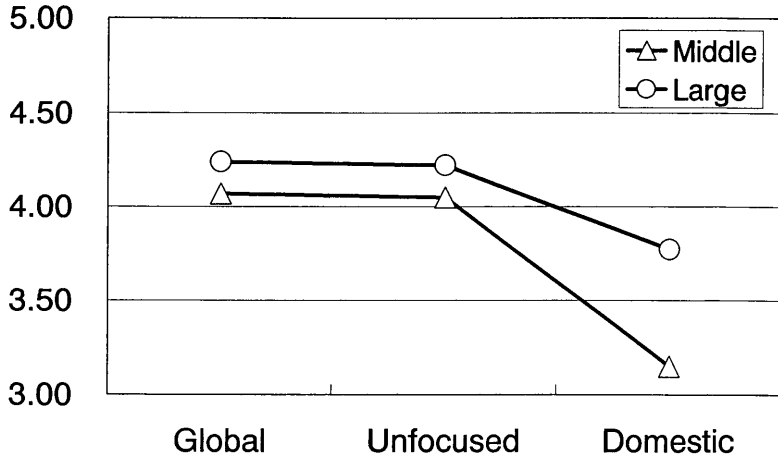


Figure 4-6 : Enhance international rotation of personnel

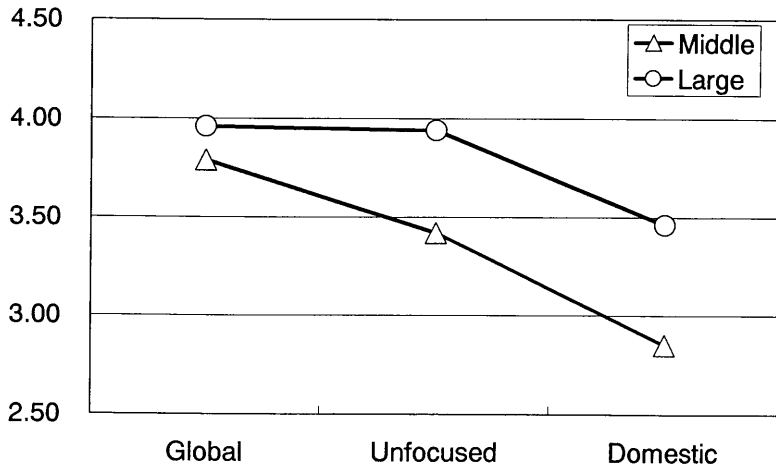
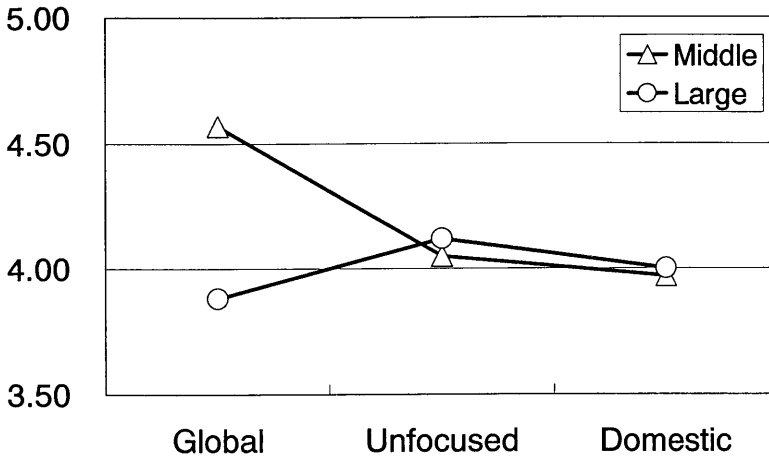


Figure 4-7 : Compensation in accordance with personnel evaluation



for overseas subsidiaries” and “enhance international rotation of personnel” are statistically significant (Figure 4-5, 4-6.) In either of two items, large-sized firms were more aggressive than middle-sized firms and “Global” companies were more aggressive than other types of companies.

Interaction effects were found in “compensation in accordance with personnel evaluation”. Among “Domestic” or “Unfocused” firms, there are no significant differences between large-sized and middle-sized firms. However, in “Global” firms, middle-sized companies’ compensation scale seems to be more performance based than large-sized companies (see Figure 4-7.) This would lead an argument that “middle-sized Global” companies globalize through intensive internalized incentive system..

5. CONCLUSION - The Need for Middle-Sized Manufactures to Change their Global Strategies

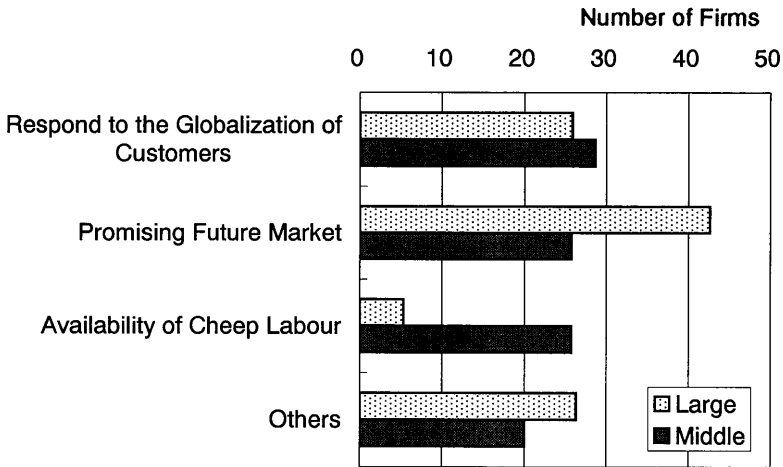
5-1 Globalization of Large Scale Assemblers

Although many Japanese manufacturers established their production facilities overseas, their global expansion was strongly controlled by the HQ in Japan. However, since the arrival of fierce global competition during the mid 1990's, known as the "Mega-Competition", those companies which placed great importance on overseas expansion started to take on a different view. They no longer viewed overseas expansion as an alternative location for production sites, but as operations with their own autonomy. By coordinating these operations, they are working towards globally strengthening the integration and the competitiveness of the group as a whole. At the same time in regards to the flow of technological information, know-how, and human resources, the direction of the flow is shifting from the traditional one-way direction from HQ. More and more of these information and resources are flowing from subsidiary to HQ, and between subsidiaries themselves at a multi-dimensional level. Traditional concept of employee transfer was very HQ orientated. However, a new system is in the process of forming, placing a higher value on global rotation of employees and interaction.

Global strategies adapted by large Japanese companies, as mentioned here in recent years, can be interpreted as the development stage of globalization as advocated by Bartlett & Ghoshal's "Transnational Companies". In other words, as well as achieving higher efficiency on a global scale, it accomplishes coordination of information and resources provided by every region. By reducing the information gap between these regions, a company can achieve a true competitive edge as a global company.

Having experienced the physical nature of globalization by

Figure 5-1 : Reasons for Globalization



Source: Ministry of International Trade and Industry (1997)

establishing production facilities overseas, Japanese companies are now entering a new stage of globalization. By making a conscious effort to improve the coordination between all regions, new information and knowledge generated in the process are utilized to give them further competitive edge.

It is also a fact that increasing number of companies, which are expanding overseas, aggressively engage in alliances and joint ventures with local companies and internalize the knowledge and resources gained. In an environment that is rapidly evolving, it has become increasingly necessary to cooperate with skilled local companies in order to achieve competitive edge at a global level.

5-2 Globalization of Small and Middle-Size Companies

A question to be asked is whether this new wave of globalization is only applicable to large scale manufacturers only.

During the 1980's and 1990's, number shows that surprisingly large number of small and middle-sized Japanese companies have expanded overseas. However, the nature of their expansion was more as a result of following and supporting larger companies and fulfilling their role as suppliers, in contrast to a case of self led expansion. They are expected to provide parts with the same specification and quality as the domestic operation. Therefore their mission is to precisely follow orders from the HQ in Japan. Naturally, subsidiaries were not demanded to provide to the HQ technologies, know-how, R&D, and original ideas on production process from their local operations. Occasionally specifications were adjusted to local standards. However, there were no instances of changes in specification which directly contributed to the competitive edge at a global level.

In a sense, the relationship between these parts suppliers and local clients (being the subsidiary of large Japanese assembler) was indirect, because it was coordinated by the assembler's HQ in Japan, who had the authority to coordinate their subsidiary. Therefore the degree of direct involvement the two local entities had with each other was minimal. As seen already, this explains the reason why small and middle-sized manufacturers, although they may well have expanded globally, tend to focus their resources to domestic R&D efforts, rather than to R&D efforts overseas.

To summarize, many of the small and middle-sized manufacturers, which expanded to the global market, did so only physically by following large scale assemblers, who had the ability to achieve competitive edge in the world market. In was a global expansion without any consideration to the diversification of the end user market, nor with any further consideration to customers' needs. Therefore it made no sense to expect any transfer of knowledge and know-how from the subsidiaries to the HQ.

While the business globalized however, large-scale assemblers began

to lose its competitive edge in the wave of “Mega-Competition”, and the existing global system was forced to be reevaluated. Local subsidiaries of large scale assemblers began to increase their independence from the HQ in order to better respond to the local market. At the same time they established themselves at a globally competitive level by achieving global operational efficiency. As a result, it became difficult for the small and middle-sized parts manufacturers to maintain business relationships with the subsidiaries indirectly through the HQ as they had been doing.

5-3 Global Dilemma Faced by Small and Middle-Sized Companies

What development process will apply to the globalization of the small and middle-sized Japanese companies?

It has already been mentioned that global strategy of small and middle-sized Japanese companies were traditionally only that of physical expansion as a result of following large customers. However, as the global competition intensified, and subsidiaries of large assemblers gained autonomy to overcome the tougher competition, it had become critical for small and middle-sized manufacturers to respond to the local market accordingly. Under these circumstances, unless an independent and a fast decision making process is adapted, it would not be possible to compete against the local competitors and win. In order to maintain an independent business relationship with the local subsidiary of large assembler, even the small and middle-sized manufacturer has to achieve the ability to make independent business decisions for the local market.

However, there is a question as to whether the existing global strategy, which had been proven for large corporations, will be also effective for small and middle-sized manufacturers.

First of all, there is a risk of diversification of management resources by increasing the independence of the local operation. Up until now, due to the geographical expansion of operation, small and middle-sized

manufacturers had been diversifying their resources overseas. It can be argued that there is a long term benefit of educating employees through overseas assignments, however it also has to be agreed that there are disadvantages to spreading scarce number of employees overseas. In addition, diversification of capital investment does have some benefits such as the diversification of risks. However, there is likely to be some overlap of investments, and at least the benefit of economy of scale is sacrificed to some degree. Indirect cost can not be ignored either. For small and middle-sized manufacturers, who do not have the luxury of plentiful resources that the large assemblers do, diversification of resources can be a huge obstacle against global expansion in the future.

The second factor to be considered is the possibility of changing the existing nature of the business relationships with clients. To increase the autonomy of the local operation means not only increasing local data base and diversification of activities, but also changing the nature of the existing relationships. The new framework of relationship, which goes beyond that of the existing relationship, will likely bring both positive and negative effect to the existing client. When the benefit to the client is obvious there will be no problem. However, when the benefit is to be realized over long term and it is not obvious, there is a possibility that the relationship with the existing client is forced to be terminated. Such dilemma is a topic left to be solved by small and middle-sized manufactures, who originally expanded overseas by following large assemblers.

The third is the dilemma created by the traditional global strategy, which was based on integration of the HQ and subsidiary. As already discussed, under the traditional global management of small and mid-size manufacturers (followers of large assemblers), priority was placed on domestic R&D and innovations were developed by the HQ and transferred to overseas. Consequently, a strategy centered around the HQ was formed,

and the decisions for and the evaluations of the overseas subsidiaries were made by the HQ. Such was the foundation on which the success of the small and middle-sized manufacturers was based on. However, the increased autonomy of the subsidiary will encourage the diversification of the local operation. This will contradict with the traditional centralized global strategy, which strongly emphasized integration. Ironically, the very same system that led the small and middle-sized manufactures to success in the past will create a dilemma for future globalization.

Whether they like it or not, Japanese companies must face global competition. Changes in the market environment force changes in the Japanese business systems, and this invalidates the traditional business system which had been effective in the past. This is best represented by the dilemma faced by the Japanese manufacturers, which expanded overseas following their large-scale customers.

It is a difficult task to solve this dilemma, however without doing so the future survival of the Japanese companies is doubtful. A true strategy is to adapt a long-term vision and solve various dilemmas that the company faces. It is nothing but this exact process of coming up with specific plans to solve these dilemmas that is required as the process of business development.

This article fell short of coming up with such specific plans, and it will be left as a research topic for the future.

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