INTERNATIONAL MARKET ASSESSMENT-ASIA PTY LTD

Asian Issues Management Paper

Confidential

Structuring Asia/Pacific Operations, 2004

China's challenge to regional management

This **Asian Issues Management Paper** is based on a presentations and discussions at IMA Asia's briefings in May (by Chris Nailer) and August 2004 (by Michael Boyden and Chris Nailer). It also draws on an AIM Paper from March 2000 on Organising for Asia Pacific by Michael Enright and a paper for the National Graduate School of Management at ANU on Managing Asia's Strategic Regions written by Chris Nailer in June 2004.

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Asian Expertise

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Structuring Asia/Pacific Operations, 2004

China's challenge to regional management

Five propositions for structuring A/P operations in 2004

- **Management strategy in Asia now focuses as much on how processes are done as it does on the structure of operations.**
- **China's rapid emergence as a global production site and a global market is forcing a major rethink of regional management.**
- **The Greater China structures (China, HK, & Taiwan) established over the last decade are no longer useful.**
- **Shanghai is becoming a viable Asian RHQ site for some firms and could dominate within 10 years.**
- **The rest of Asia will require increased management attention as Japan revives, India opens up, and Asean gradually gels as a major sub-regional market.**

Earlier reports on structuring Asian operations

A number of reports have been produced over the last 25 years on structuring Asia/Pacific operations, initially by Business International and more recently by Professor Michael Enright at HK University. This AIM Paper examines current trends in structuring and suggests how China's rapid rise as both a market and production site may trigger another wave of restructuring for MNC operations in Asia. The analysis is based on interviews with clients and peer group discussions over May to August 2004 carried out by Chris Nailer and Michael Boyden. It also draws on a research paper by Chris Nailer on Managing Asia's Strategic Regions (National Graduate School of Management, ANU, 2004).

Key structuring questions in 2004

The main questions that clients put to us as we sought an update on trends from the earlier work were:

- **Regional management** – are RHQs still needed and, if so, where are they being moved to, what functions do they contain, can the roles be dispersed across the region or do they need to be centralised, can you run Asia from Shanghai?
- **Sub-regions** – should Asia be segmented to improve management focus and, if so, how?
- **Country heads** – where companies have given primary authority for business management in Asia to product or customer divisions is there a case for maintaining country heads who control all divisions in large complex markets like China and India?
- **Back office and support functions** – where are the best locations for different back office functions?

Strategy + corporate politics = structure

Corporate structure - capturing opportunities & dealing with problems

Corporate structure's main aim is to help companies capture opportunities and address problems. Over the last 25 years we've observed that corporate structures tend to change more rapidly in Asia – we'd estimate a major change every three years - than structures in other regions, which reflects rapid shifts in the region's opportunities and problems.

Structure also reflects corporate politics

Corporate structure is also about corporate politics, which can range from beneficial to benign and sometimes to destructive. As this varies widely by company we have only two comments on the role of corporate politics in structuring regional operations. The first is that no organisational structure should ever be seen as set in stone. Given the apparent speed of restructuring in Asia it's important that managers remain open to regular re-assessment of existing structures rather than defending the existing structure or claiming the latest reorganisation is the best (it might only prove suitable for the next two years). The downside of this is a considerable amount of personal turmoil for some executives (and for some families) during a restructuring. However, clients have also emphasised that well-managed restructurings do capture targeted benefits as well as reinvigorating regional businesses.

… and personalities with specific skills

Our second observation is that personalities are a critical factor in corporate politics and thereby in corporate structures. A number of our clients note that some structural decisions were made to tap the skills of one of two specific managers without requiring them to relocate. Generally this means the shifting of some reporting lines and possibly the addition of one or two additional regional support staff in a particular location. However, we've noticed that such personality-driven structures only last one to two years at most, particularly in those cases where travel is difficult, support services are weak, and key markets or regional operations are at a distance.

Organisational structures in Asia/Pacific

Before looking at how companies are changing their structures it is worth briefly looking at how the existing structures emerged. IMA Asia has covered regional business structures in a number of briefings over the last 12 years. In the most recent of these (March 2000) Professor Michael Enright from Hong Kong University summarised the state of play for corporate structures in Asia at the end of the 1990s based on some 350 interviews and over 1,000 survey results gathered over 1998-2000.

Early entry structures: hub & spoke

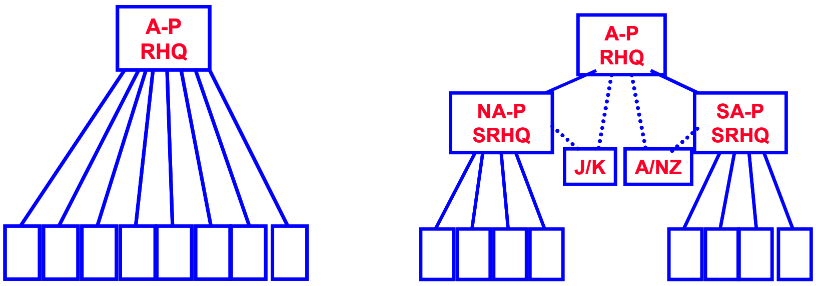
Hub & spoke worked well for new operations in emerging markets

… with major barriers to cross-border integration

The most common management structure over the 1960-1985 period was a central regional headquarters (RHQ) with a large staff controlling all country operations with relatively thin senior staff allocations in those country operations (in some cases just one expat, which might have been all that was allowed by local employment laws). Some country operations where distributors or licensees because of sub-optimal scale for investment or entry restrictions. The Asian RHQ provided extensive support services to the country operations in marketing and sales, finance & tax, legal & regulatory, logistics, and HR. There was very little, if any, cross-border interaction between country offices, which largely reflected the extensive barriers to cross border trade with some exceptions (e.g. the informal Singapore-Indonesia relationship).

Sub RHQs helped focus management on key local markets

Traditional geographical reporting structures for MNCs in Asia
Source: M Enright, 2000



Hong Kong was the dominant RHQ

… Singapore's rise as a RHQ site from 1985

From the 1950s to the late 1980s Hong Kong was the dominant site for Asian RHQs. By the 1980s, however, a significant number of MNCs were establishing sub-RHQs to focus management resources on specific geographies. Singapore was the greatest beneficiary of this trend with a rapid rise in RHQs (primarily sub-regional but also some regional) over the 1980s. Singapore's primary advantages were – and remain - its central location in Asean, excellent infrastructure, attractive incentives, and lower cost structure than HK.

… plus a few RHQs in Japan & Australia

In addition, Japan and Australia each gained or retained around 5% of the Asian RHQs based on their large domestic markets with the associated benefits of a large pool of country resources that could be tapped as needed to assist regional management. However, both Japan and Australia also had disadvantages: in Japan's case its sheer size and market complexity tended to capture most of the attention of regional managers operating from Tokyo; in Australia's case distance from other regional markets is an issue.

… and some Asean RHQs in KL, Manila & Bangkok

During the late 1980s and early 1990s a handful of RHQs were also established in locations like Kuala Lumpur, Bangkok, and Manila. These were partly driven by cost considerations and the benefit of support from large local country operations for some firms. Rather than being full A/P RHQs they tended to be sub-RHQs for Southeast Asia.

Plus the growth of country offices in Asia's 1990-96 boom

By the early 1990s rapid growth in many East Asian markets had also enable relatively large country management structures to be developed, particularly where an easing in foreign ownership restrictions had enabled wholly-owned ventures to replace JVs or distributors. Moreover rapid sales growth over 1990-96 tended to mask a build up of management cost at both the country and regional levels.

RHQ incentive packages

… had little impact on structuring (except for Singapore)

From the mid 1980s on a growing number of regional governments attempted to win RHQs by offering incentives and favourable operating conditions. The best of these appears to have been Singapore's Operational HQ (OHQ) status in terms of its combination of tax incentives and excellent operating conditions. Others also offered tax breaks but by-and-large most other RHQ incentive packages mainly reduced the burden of red tape and excessive taxation in a country's normal operating environment.

Hub & spoke structures

… key benefits

The key benefits of the hub and spoke system were:

- An ability to run minimal country management offices.
- Strong top management cohesion and quick decisions.
- Efficient utilisation of centralised regional support services.

… and drawbacks

The main drawback of the hub and spoke system were:

- Minimal in-country development paths for good country staff.
- Little focus on cross border synergies.
- The high cost of maintaining mangers and centralised services, particularly in locations like Hong Kong.

Hub and spoke RHQs remain useful structures for companies that are relatively new to Asia and are focused on entering markets and building operations.

The rise of networked regional management in 1990s

The 1990s saw a dramatic restructuring of Asian operations due as much to global factors as to developments within the region. By far the most important of the global factors were:

The global rise of matrix management

… thanks to the WTO

… and major improvements in IT

A global move to matrix management. The contest between product or customer-focused divisions and geographic managers has waxed and waned for decades. In the 1990s it surged again driven by a need to slash management, production and logistics costs and, for some companies, to address a globalisation of their customer base. The globalisation of markets under the WTO was a key aspect of this development.

Major improvements in IT. Prior to the 1990s efforts to establish product or customer division management as a primary or co-equal global framework usually collapsed because of reporting difficulties and span of control issues. By the 1990s dramatic improvements in IT enabled real-time management and support for global product and customer divisions. Matrix management is here to stay.

The main changes affecting structure within the region were:

PLUS - Asia lowers its barriers to cross-border business

Reduced barriers to trade , investment and expats. Reduced barriers to investment led to a move to wholly owned operations. Tariff cuts under the WTO process and the various Asean schemes enabled easier cross-border flows of products. Restrictions on expats were

… and the Asia Crisis requires massive cost cuts

also eased as countries competed for regional management / back office functions (the latest example of his is China's decision in August 2004 to start issuing 10-year residency permits to "high-level" foreigners – not quite what a typical expat executive wants but a step n the right direction).

The Asia Crisis. This prolonged slowdown in regional growth forced companies to look for options to slash regional overheads. RHQs and sub-RHQs were cut back, relocated or closed with their functions being distributed around the region.

The result -

In our Mach 2000 briefing Michael Enright described the changes this forced on MNC organisational structures in Asia.

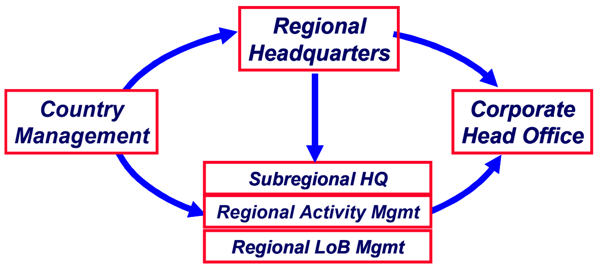
… a major reallocation of authority & responsibilities in Asia

Global HQ's reclaimed power from RHQs and country operations. Primarily via the introduction of matrix management and powerful enterprise management software systems.

The demise of country managers. The all-powerful country manager lost authority and responsibility becoming, in Michael's words, often little more than "the Building & Grounds Manager."

RHQs were tending to atomise. The support functions were distributed around the region to lower costs, tap local areas of expertise, and build careers for good second tier country executives. The RHQ that was left became little more than the regional CEO and his secretary. Regular regional management meetings were held by flying in to central locations or moving around the major regional operations in rotation backed up by video conferencing.

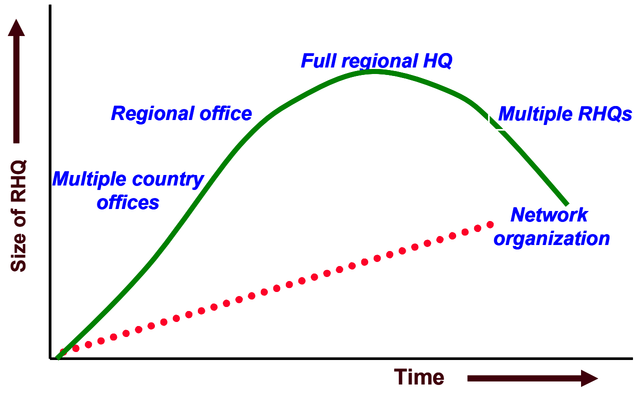
1995-2000: Matrix management shifts authority & responsibility in Asia
Source: M Enright, 2000



The rise of "networked organisational" structure in Asia

As a result, Michael Enright found that by 2000 most of the MNCs with large Asian operations had tended to follow a path that started with a few country offices, followed by a large RHQ, before eventually restructuring in the late 1990s to a networked organization. Michael's contention was that by 2000 some MNCs that were relatively new to the region could skip the build-up to a full RHQ and go straight to a network organisational structure.

Typical life cycle of RHQs in Asia up to 2000
Source: M Enright, 2000



Network A/P structures

… key benefits

The benefits of networked organisational structures are:
- Fits with global matrix structures.
- Fits with regional trends to lowering of barriers to cross-border business.
- Highly adaptable and thereby tends to align better with the actual flow of business and support services around the region.
- Builds stronger regional team play down into mid-level country managers.
- Removes cost of maintaining a RHQ.

… and drawbacks

The drawbacks of network organisational structures are:
- Loss of ad hoc discussions and quick decisions around the water cooler in the RHQ.
- Possibly higher travel costs as all the various regional management teams get together, although this was probably coming due to the rise of matrix management and the lowering of cross border business barriers.
- Some individuals find it hard to adjust to multiple tasks.

The focus shifts from structure to regional processes

Focusing on the processes reconfirms networked structures

Chris Nailer's interviews in 2004 bring to light some of the latest changes to MNC's views on regional management. As Chris notes, "Asia Pacific management coordination today is a lot less about structure, and much more about process." Of the five major trends raised with Chris during his interviews four were more or less to do with how key processes were performed in the region (the four are briefly described below). This is not so much a case of the emergence of a new management structure for the region as a decline in the perceived importance of structure as a primary element of regional strategy. Deciding how best to do a variety of functions and then locating them in appropriate areas is a hallmark of the networked structures outlined by Michael Enright in 2000.

… and the suitability of many sites in Asia

The shift in focus from structures to processes inherently recognises that Asia now has many locations that are suitable for a wide range of support, back office and management functions. Early contenders for call centre and back office work like the Philippines and Australia are now challenged by India and surprisingly several locations in China. Equally surprising has been the rise of Shanghai as a location for senior regional managers – not yet quantified but apparent in many of our interviews.

1. A move to cross-border value chains

The growth of intra-regional business

Under the WTO process the region as a whole is increasingly becoming part of a single, globally integrated value chain with very few countries left with entire value chains. The main variations on this are:
- Asean's gradually emerging trade block, which is encouraging sub-regional value chains that focus on the main Asean markets.
- A few remnant country value chains, typically in India and Japan, where

regulatory or infrastructure barriers make it more sensible to have complete value chains within the country.

- Highly regulated industries.

Re-thinking how business is done

2. Polarisation of functions

Increasingly companies are separating customer-facing activities, which are being driven down the path to greater localisation, and support/coordination activities, which are being taken away from country-level managers and brought together in regional centres and, sometimes, global centres.

Locating regional champions

3. The rise of regional manufacturing and centres of excellence

Just as manufacturers are being driven to find scale efficiencies in Asian production some are also being driven to do more local innovation. This is leading companies to nominate centres of excellence or innovation within regions. The location of these centres varies by product group within a company.

India has changed the global back office

… as China has changed global manufacturing

4. India's rise as a global back office & technology support location

India's rise as an emerging market has had a big impact on regional management, creating much more arduous travel schedules for regional executives and contributing to growth in Singapore RHQs (as Singapore has some of the best and shortest airline connections into India from the east). However, India has had an even bigger impact on global strategy through its rapid development as a global centre for Business Process Outsourcing (BPO). India's claim to global status in this role automatically shifts the balance of resource allocation within the Asia/Pacific region in much the same way that China's claim to pre-eminence is some areas of manufacturing shifts the balance within Asia for manufacturing and logistics planning.

China's challenge to regional management

Shanghai is becoming the de facto Asian RHQ for a growing number of MNCs

The fifth development raised during Chris Nailer's interviews was the dramatic rise of China as both a market and a production site. This is the development that looks set to bring the next wave of change to how MNCs manage their regional businesses. Many of our interviewees described modifications to their regional structures in an effort to cope with the demands of the China market. It was striking how many times we were told over the last month that a senior manager based in Shanghai was the acting or de facto Asian head. This appeared to be most often the case because the company's most senior manager resident in Asia had moved to Shanghai to lead the development of the China operation.

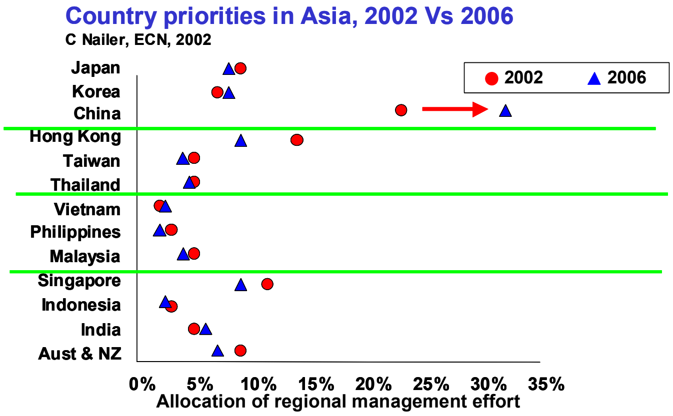
How does China vary from Japan?

This is not a re-run of Japan …

As Asia/Pacific structures have already had to adjust to one economic superpower – Japan, still the world's second biggest economy – the first obvious question is how does China's rise differ in its impact on MNC strategy in Asia? China does vary in two crucial ways.

… as China has a much bigger demand on top management time

(1) The demand on senior management time. The first is the amount of senior management time (both regional and global) that is being devoted to China. The Economist Corporate Network's regular polling of regional managers in Singapore and HK over the last few years shows an astounding level of senior management concentration on the development of the China market. It is doubtful whether Japan ever received the same amount of attention at any time in the last 40 years.



Source: Economist Corporate Network, Survey of Singapore and Hong Kong Regional Business Groups, September 3rd & September 5th-6th 2002; N=206 respondents

… and China's demand on management time will increase

The chart above is based on a survey in September 2002 of just over 200 clients in regional offices in Singapore and HK. Even then China dominated, receiving a quarter of all senior regional management time. The expectation was that this would rise to one third or more of regional management time by 2006, with the time allocated to all other markets being cut back with marginal exceptions for Korea, India and Vietnam. These 2002 estimates of expected allocation of effort by 2006 may be understated. By August 2004, China was moving forward on its market opening commitments – particularly in areas like distribution – more comprehensively than many had expected. Moreover its ability to sustain relatively high growth appears to have improved. Both these developments point to a rapid development of the market over the four years leading up to the Beijing Olympic Games in 2008, including the opening up of the finance sector from the end of 2006.

China is also reshaping global manufacturing

… in a way that Japan didn't

(2) China's manufacturing capacity. Most Western MNC found remarkably few linkages between their production in Japan and the manufacturing and sales operations elsewhere in Asia. Typically what was manufactured in Japan was for the Japanese market while Japan's thicket of non-tariff trade restrictions have made it very hard to ship from other factories in the region into Japan, although these barriers are easing. As a result, Japan's leading export brands are Japanese owned while China's exports are dominated by Western MNCs.

… leading to the "China + 1" syndrome in manufacturing

For many global manufacturers China is now the primary market for capacity expansion. As one executive told Chris Nailer, "When a proposal to increase manufacturing is tabled anywhere in the world HQ's immediate response is to say 'tell us why this plant shouldn't be put in China'." Over the last five years this has become known as the "China + 1" syndrome in manufacturing in Asia. With trade barriers falling and China becoming the main manufacturing site in the region for many industries most MNCs can see the need for only one other production site in the region justified primarily by the need for an alternative supply point in the advent of problems in China.

As a result, China is becoming the hub for regional commerce

One result of China's rise as both a market and global production site has been a dramatic rise in intra-regional trade as MNCs started shipping components and materials from elsewhere in Asia to their factories in China. This process will be given a major boost over the next few years by two major developments:

… watch the impact of China FTAs over the next five years

- The opening up of China's distribution system so that foreign firms can take control of distribution of overseas made products inside China; and
- China's intention to sign bilateral free trade agreements (FTAs) with most of the other significant markets in Asia. The most notable of these is a bilateral FTA with Thailand (with could prompt massive trade flows between the rapidly developing automotive sectors in both countries) and the China-Asean FTA.

By contrast, Japan was often on the periphery of regional structures

As a result of these differences many more Western MNCs placed Japan on the periphery of their regional management structures over the last 40 years than placed it at the centre. In fact two structures typical of our client base over the last 40 years were:

- Japan as a large and strategically important market was made a direct report to Global HQ with minimal interaction with the rest of the region;
- Japan as the black hole on the map with surprisingly little business.

Coping with China's rise: The Greater China solution

Staffing needs for China drove Greater China structures

Most Western MNCs ran their early China operations from Hong Kong in the 1980s. But by the end of the 1980s it was clear that China's enormous demand for management skills required a new solution. This lead to the creation of Greater China regions within many MNCs that combined HK, China and Taiwan under one sub-regional management team. The great advantage of this structure lay in tapping suitable human resources, specifically the ability to draw on a large pool of Mandarin-speaking managers with strong Western business skills from Taiwan. It also enabled some centralisation of support and back office services. For some companies there was also the useful public affairs benefit that the firm's Greater China region accorded with Beijing's view of how the world should look.

Two companies interviewed by Michael Boyden illustrate how the Greater China structure worked for many MNCs over the last 15 years (Taiwan Case 1) and how it was modified to cope with the introduction of matrix management structures in the 1990s (Taiwan Case 2). It is notable in the first case study that Greater China was not based on similarities in customers, a situation that we think is typical of how most companies see these three quite different markets.

But in market dynamics

… HK, Taiwan and China are very different

Taiwan Case Study 1: Classic Greater China
(FMCG firm)

Structure and strategy
- A large and well-developed Taiwan business and an emerging China business (via a local JV) are run separately.
- China's potential is recognized and there will be investment in brand equity but not yet in infrastructure and people.

Taiwan's role
- Taiwan contributes HR, marketing skills & training to China with the aim of achieving local self-sufficiency.
- But Taiwanese consumer behaviour may not serve as a model for the China business.

Future
- The cross straits links situation is crucial. Absent direct links, the Taiwan and China businesses will continue to be run separately.

M Boyden, TASC

China business now dwarfs Taiwan & HK for many companies

Taiwan Case Study 2: Greater China – adapted to matrix management
(Chemicals, industrial goods, and life sciences firm)

Structure
- AP matrix structure with both country heads & business heads.
- China MD, based in Shanghai, speaks for GC in both geography and businesses.

Sales & investment
- Taiwan = 25% of GC sales. A stable business but no longer considered strategic and declining in relative importance.
- Investment in AP heavily focused on China. A proposed large investment in Taiwan was torpedoed by local politics.

Future & key issues
- Taiwan likely to remain largely autonomous, especially in such locally-focused business as life sciences.
- The absence of cross straits links is a pain but especially irritating in the HR aspect.

> - Taiwan will remain a significant knowledge contributor to GC but China businesses are rapidly becoming self-sufficient.
>
> M Boyden, TASC

Why Greater China is dissolving

The first two Taiwan case studies not only show the HR focus typical of Greater China structures but also highlight the three big issues that are leading to the demise of Greater China structures:

(1) China's economic dominance

China's rapid rise in market size. For many MNCs China is no longer an emerging market on par with other East Asian markets. Many companies now find that their China sales – and operations - are many times bigger than those in Taiwan and HK combined.

(2) Shanghai's growth as a China or A/P HQ

Shanghai's rise as an office location. With its new airport, copious amounts of new nigh quality office space, eased restrictions, and good quality staff Shanghai is rated as a good office location even though support services and airline connections are not equal to those of HK.

(3) No direct flights from Taipei to China

Cross Straits Links (CSL) are stalled. Over the last 20 years companies have hoped for direct flights between Taiwan and the mainland. But the political barriers to such flights now seem bigger than ever and companies are tiring of the time-consuming and expensive connections via a third country (typically HK).

Rethinking Greater China means rethinking Asia

Two final Taiwan case examples illustrate how some companies may position Taiwan and China in the regional structures in future. Taiwan Case Study 3 highlights the way in which MNC are now rethinking the entire structure for Asia Pacific as the Greater China structure dissolves. In common with quite a few of the companies we've talked to this company is working within a matrix structure to create product-based business groups that run across the region while also looking at a sub-regional geographic structure to enable management resources to be focused on North Asia. Two other striking features are that the regional MD is now based in Shanghai (a growing trend) and that consideration is being given to a sub region that combines China and Asean (which is quite unusual but based on the dominance of Chinese business practices, which is a significant factor in the market for this company).

One option –

Putting the Asian MD in China

… with sub-RHQs for North and South Asia

Taiwan Case Study 3: Greater China Dissolves
(Health care, consumer and industrial products firm)

Greater China sales
- China sales dominate in GC (90% of healthcare and 60% in graphic arts). Total Taiwan sales are 20% of GC sales.

Structure and restructuring
- GC used to be an administrative and operational region within the AP structure but is 'dissolving' now.
- There is no longer a GC general admin function and the MD in Taiwan reports to the MD for AP instead of an MD for GC.
- 2 of the 3 business groups in GC have been combined with those in ASEAN to capture synergies. The third is still "GC" but will be moved into North AP by the year end.

Future
- Emerging North Asia (Japan, China, HK, Taiwan, Korea) and South/SE Asia structure. Put SE Asia with China? China MD already speaks for all AP.

M Boyden, TASC

Taiwan remains a strategic market for a few companies

Taiwan Case Study 4 is a useful reminder that for some MNCs Taiwan will is still a strategic market in its own right without any need to refer to the current or potential scale of operations in China. This is particularly the case where Taiwan has globally significant local players in an industry. Although our case study is from the building materials sector this would aptly apply to the IT sector where Taiwan has a number of globally significant competitors.

Taiwan Case Study 4: Taiwan as a strategic market in its own right
(Building materials firm)

Current structure
- Taiwan - a maturing production and trading business in Taiwan that is seen as key to their Asian strategy.
- Only now beginning to look at China – but through the eyes of the former country head in Taiwan.

Strategy considerations
- Taiwan is still a strategic market, partly due to the current and potential future clout of the Taiwanese players in the industry.
- As a mature market, Taiwan is no longer high on the list for investment…but China potentially is.

Future
- Going forward they will be run separately but within an AP regional structure.
- Taiwan will contribute HR, contacts, cultural nuances, skills.
- The CSL situation has "no practical impact" as yet. Absent improvement, they could well find it a pain in the neck later on.

M Boyden, TASC

Ultimately the demise of Greater China is due to the rise of China as a regional commercial and management hub, which makes it hard to operationally treat China as simply the biggest part of a 3-country structure that groups it in a small sub-region with Hong Kong and Taiwan.

What next? Polar or Bipolar Asia structures?

The key trends from the last decade continue to evolve

Before looking at the structural options that are emerging in Asia and also replacing Greater China structures it is worth identifying the elements of regional strategy that look set to remain in place through the next decade. These are:

Matrix management – this suits the way global markets now work under the WTO and is cemented in place by ERP systems.

Networked regional structures – The biggest consideration here is the need to create flexible cross-border teams that address cross-border objectives.

Lean management hubs – Where management hubs exist they tend to be multiple rather than single and are lean with just a few regional support and management functions in each hub. The exceptions to this are regional entry operations.

Centralised support – Cost and technology considerations will continue to drive this process. While Asia has been more a seller than a buyer of outsourcing over the last decade the next decade should see rapid growth in outsourcing within Asia.

Cross-border value chains – The next five years will see a rapid drop in most of the remaining barriers to trade in Asia. Companies will continue to move to fewer, larger factories while at the same time spreading components of the value chain across several markets driven by efficiency and competitiveness considerations.

China + 1 in manufacturing – In an extension of the cross-border value-chain development many companies will increasingly locate their main Asian production in China with one other major operation elsewhere in Asia.

The challenge of the Rest of Asia

If it comes down to these five factors plus the rise of China's economy then within this decade China will move from being the de facto RHQ in Asia for a handful of firms to being the regional head office of choice. The problem with this scenario, as Chris Nailer points out, is what to do about the rest of Asia (ROA), which also happens to include two or three other markets that are set to claim strategic status for MNCs, including India, a revived Japan, and Asean (provided it continues to consolidate as a free trade area). It is unlikely that regional managers based in China will be able to devote sufficient time to other opportunities in north and southeast Asia let alone in India.

China + 1 also applies to regional management

This tension was already becoming apparent in the interviews we conducted in 2004 with a number of companies establishing - or re-establishing - sub-RHQs to cope with the span of control issues. No one pattern appears to be dominating, which is what might be expected within a networked environment. Hong Kong and Singapore are still the main locations for regional managers but some of the other options we noted were:

China + 1 – just as this applies to manufacturing in Asia it can also apply to management. In this case the top AP manager sits in Shanghai with a second management hub outside China covering either ROA (the rest of Asia) or a sub-region such as Southeast Asia, in which case the Shanghai-based manager also covers North Asia.

Two sub-RHQs – The typical split is North Asia (usually run from HK but Tokyo, Taipei and now Shanghai are also contenders) and Southeast Asia (usually run from Singapore although Bangkok, Sydney and KL are also contenders). The top executive for Asia need not reside in either of the hubs but may be in a third location in the region (this was the case for those firms who noted that the de facto regional head happened to be the GM in Shanghai).

Are country heads needed for China and India

… or should these massive markets be broken into regions?

On the issue of whether a single country head is required for complex emerging markets like China and India most of the MNCs we spoke to still favour a strong country head even though they have disappeared elsewhere in the region. This appears to be as much because dealing with local regulators and partners requires it as any other factor. However, there are also signs that this exception is starting to disappear. Several of the largest MNCs in our client group have up to a dozen different divisions running in China with minimal coordination. Moreover at least one firm with a number of significant operations in China treats China as a number of regions that reported individually alongside other country operations in Asia

Rebuilding regional management in Asia

Does the discussion above suggest we are seeing a reversal of the stripping down of regional management that occurred over the last six years? Cutting management costs has been a tenet of regional management since 1998 as neither sales growth nor strategic prominence justified a build up in resources. Corporate sentiment now appears to be moving back towards committing resources to capture a share of Asia's strategic markets. China clearly dominates the strategy list in Asia at present but other contenders are emerging forcing companies to address span of control issues as they rebuild regional management teams.