

# Rotterdam or Anywhere Relocating Corporate HQ



Offshoring is the buzz concept of the noughties. But no matter how much the material business is diverted to other countries or even continents, headquarters are invariably located where the company originated – sometimes in out-of-the way towns and small cities.

But, as **Marc Baaij**, **Douglas van den Berghe**, **Frans van den Bosch** and **Henk Volberda** point out, there are many cases where the case for relocating headquarters is excellent. So why doesn't it happen? Is it inertia, operational difficulty – or just that the companies haven't thought of it?

The paradox of the global corporation is that while most value adding activities relocate when the environment is right for change, the activities of the headquarters remain at their original location. A glance at the Fortune Global 500 corporations reveals that only one cross-border relocation took place in the decade from 1994 to 2003: the Chrysler headquarters, relocated from the US to Germany in 1998 after the cross-border acquisition by the German firm Daimler.

This is the exception that proves the rule. Most companies appear to believe that the activities taking place at the headquarters are exempt from the forces of internationalisation. But this is strange when one considers that otherwise, internationalisation forces are so all-pervasive. The first element of the corporation to internationalise was sales, then manufacturing. Currently, we are in the midst of the internationalisation of activities of higher added value – research and development and corporate services, to take two examples.

The lowering, or even elimination, of trade and investment barriers combined with the increasing sophistication of ICT and transportation technologies enables corporations to slice up their value chain of activities more finely. They can then optimise the geographical location of each individual value adding activity.

With the ability to make activities mobile and cross-country wholesale moves so necessary, and so effective, why have corporate headquarters remained untouched by the forces of internationalisation? Changing the location of the other activities isn't without consequences for the chain of command and control of the corporation – i.e., the corporate headquarters. Having optimised the locations of their value adding activities, corporations now need to reconsider the location of their command and control activities.

The fact is, central HQ may not be in the right place. And although this is can be an earth-

## From here to eternity

The starting point is to consider the traditional check list of HQ site selection criteria:

- Corporate tax advantages
- Investment incentives
- Investment climate
- Company law
- Operational costs
- Quality, availability and costs of the workforce
- Quality of living (major hotels and restaurants, proximity of quality housing, cultural life and recreation, quality of schools, cultural diversity, safety, crime and health factors, personal taxes, cost of living etc.)
- Level of infrastructure (in particular transportation, communication and IT)
- Level of high-level business services (e.g. accounting, legal and management consulting)
- Sufficient representative office space
- The presence of other major corporations.

The main benefit of this list is not to find suitable sites, but to eliminate unsuitable ones. Once these factors have been assessed, more strategic criteria for the right headquarters location can be considered.

## All I want is a place somewhere

To analyse the strategic motives for relocating headquarters, we need to consider HQ in a radically new light. What we currently call the headquarters is actually three different entities:

- The minimum headquarters
- The value-adding function
- The shared services headquarters.

The three have different location criteria. So if we reconsider HQ in this way, we can more effectively consider relocation.

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shattering concept for employees, it is one that should be considered like any other rational business decision.

We are therefore on the brink of a next stage of corporate internationalisation. The relocation of the untouchable headquarters can be regarded as the ultimate act of global strategy. The question now is – how do we decide where the headquarters should be?

The minimum headquarters consists of the statutory seat of the corporation and includes activities such as legal compliance, tax and financial reporting, financial control and internal audit and investor relations. It is the core and non-discretionary part of the headquarters.

The value-adding function is core as well, but it is also discretionary. It is defined as providing strategic guidance for the businesses, building and

leveraging corporate-wide competences, and facilitating synergies between the businesses.

The third part, the shared services, is also discretionary – but non-core. These elements happen to rest within the corporate headquarters because of economies of scale, scope or specialisation.

### Should I stay or should I go?

So where should the parts of the headquarters go to? The shared services part is the most mobile element of the headquarters. It does not need to be close to the business. These services can be off-shored or even outsourced as they are both non-core and discretionary.

As is now familiar, corporations relocate their shared services primarily for efficiency reasons. Common examples are relocating IT activities to

space – as Boeing did when it moved from Seattle to Chicago in 2001. Chicago was centrally located for Boeing's corporate portfolio of commercial areoplanes, military aircraft and missile systems, and space and communications.

But the first of our three thirds – the minimum headquarters – does not need to be near the value adding activities because it primarily fulfils a legal and financial role. If the value adding activities have been relocated abroad, the minimum headquarters will typically relocate from the former location of the value adding activities to a major metropolitan centre within the home country. Because of its financial role, the minimum headquarters should be close to the financial markets.

International financial clusters such as London will be attractive for the minimum headquarters.

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India and administrative services to Eastern Europe. The main criteria are: cost, quality, and flexibility of labour; cost and quality of the IT infrastructure; and tax advantages.

For corporations that relocate their shared services, economic and political risk, country infrastructure and cultural compatibility are all important considerations.

In contrast, the value adding function – the second of our three parts – needs to be located near the business end of the corporation. Originally, the value adding headquarters was conveniently located at the site of the value adding activities of the corporation. However, with the relocation of the value adding activities, the original location of the headquarters becomes out of sync with the rest of the value chain. The value-adding headquarters should, therefore, follow the corporation's centre of gravity.

In high-tech industries, the value-adding headquarters needs to be close to the R&D activities. If R&D relocates to an industry cluster, the value-adding headquarters should join them. An example is Pharmacia & Upjohn, which relocated from London to the cluster of pharmaceutical industries in New Jersey in 1999.

And in manufacturing industries, the value-adding headquarters needs to be near manufacturing. If manufacturing relocates to the largest and most important market, the value-adding headquarters should follow.

If the corporation diversifies into other businesses, the value-adding headquarters might be torn in different directions – but it should follow its centre of gravity. The value-adding headquarters may need to relocate from its original location to a more central location within the expanded corporate

Access to high level business services and the proximity of other major corporations would also be useful.

### When two become one

There are three other strategic motives that can affect the location decision of both minimum headquarters and value-adding headquarters.

- Mergers and acquisitions
- Internationalisation of leadership and ownership
- Strategic renewal.

When companies of equal size merge, they need to find a neutral location for the headquarters of the merged corporation. In 1987, ASEA from Västerås in Sweden and BBC Brown Boveri of Baden, Switzerland merged to create ABB Asea Brown Boveri. The new headquarters were not situated in either original location, but in Zurich.

In the case of acquisitions, the obvious solution is the most effective – the new headquarters is that of the acquirer, and the acquired corporation relocates (e.g. DaimlerChrysler).

Our second motive – internationalisation of leadership and ownership – makes corporations less sensitive to national sentiments or ties to a specific country. Foreign board executives and shareholders will be less attached to the traditional home country, and less likely to resist a cross-border relocation of the headquarters.

Our final reason for relocating headquarters is strategic renewal. This was a key reason for Philips Electronics' relocation to Amsterdam after 106 years of emotional ties to Eindhoven, the town where Philips was founded. Relocation can be a →

→ mechanism of change as it symbolises a fresh start and a break with the past.

## I want to break free

The reasons for relocating headquarters are sound – so why is it still only a handful of small companies who have taken headquarters relocation as an option? Part of the reason is the number of barriers that exist to impede relocation. In contrast to startups, established corporations have to deal with a legacy. In the past, investments have been made that tie the headquarters to its current location. Corporations may suffer from locational inertia – that is, the extent to which the current location determines subsequent investment in the same location.

National or regional legislation also impedes relocation. These barriers are there for good social reasons, such as the protection of local economies and the protection of jobs, especially where a region is reliant on the industry that wants to relocate. But in many countries, especially in the EU, the barriers are coming down. While this has significant social implications that are not the remit of this article, the fact is that things are changing and so companies can consider headquarters relocation more realistically than in the past.

Across the EU the situation is still complicated and it can be very expensive to relocate the statutory seat of a corporation from one member state to another. However, the European Commission is currently working on an Action Plan on modernising company law which will enable cross-border mobility of corporate headquarters within the EU.

As a result, cross-border relocation will become more and more appetising to companies contemplating the move. Shared services, being the most mobile part, will relocate first. The minimum headquarters and the value-adding function will be the next candidates for international relocation, each part according to its own strategic criteria.

## A song for Europe

We have already observed relocation of shared services to Eastern Europe and India. As soon as the European Commission's Action Plan is implemented, we may well find more examples of international mobility of the other two parts of the headquarters, the value-adding function and the minimum headquarters.

Both European management and European governments need to anticipate these upcoming developments. If a large number of companies start to shift, it could have significant consequences for national and regional economies – both positive and negative. It could be Rotterdam or anywhere – so have your parachute handy, just in case. ■

## Resources

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