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by Roger Hayter, Department of Geography, Simon Fraser University, Burnaby, 2004
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The Location of Factories as a Strategic Process

Enterprise geography (and institutional) approaches interpret factory location as an expression of the investment strategies of firms, especially large multi-plant corporations. Strategies define the competitive positions of firms in the long run and new factories are critical to this definition. Consequently, in this approach, factory location is explained in terms of the factors that influence strategy formulation. In particular, emphasis is placed on how the geography of corporate strategies is guided by 'internal' long run motivations, accumulated expertise and established corporate structures and by the 'external' strategies and structures of other business organizations, especially rivals (but also consumers and suppliers) and by other institutional forms and interest groups, notably labour organizations and governments.

Large corporations, particularly multinational corporations, are at the core of the enterprise approach (McNee 1958; Table II-1). As the dominating agent in modern industrial societies, MNCs are governed by 'technostructures,' that is professional, specialized management bureaucracies (Galbraith 1967), who have power to influence the behaviour and performance of other agents. This power is exercised in various ways and, for example, is evident in bargaining processes with other firms, labour and governments. Indeed, for MNCs in particular, location conditions and factors are not simply given datum, in the form of cost and revenue surfaces (or information spaces). Rather, wage levels and other labour characteristics, transportation rates, prices, taxation levels, the supply of infrastructure, and a host of regulations influencing spatial profitability, are subject to negotiation, persuasion and bargains of one kind or another. Technostructures are by no means omnipotent, however. Rather corporate strategies are constrained in turn
by the 'countervailing powers' of equally large rivals, labour, governments and increasingly environmental groups (Galbraith 1952).

The assertion that economic agents have power provides a different, more radical concept of the firm, the environment and firm-environment relations than that assumed by neoclassical (and behavioural) location theory (Storper 1981; see Table II-1). For Galbraith (1967), neoclassical theory represents 'conventional wisdom,' but not contemporary wisdom. Thus, in Galbraith's modern industrial economy black boxes and perfectly competitive forces exercised by 'invisible hands' are replaced by technostructures and the very visible strategies and structures of large corporations which create monopolistic or oligopolistic forms of competition (Veblen 1932; Heilbroner 1985, 1992). Moreover, in landscapes of countervailing powers, conflicts exist among economic agents who pursue goals related to security or control, market share, size and growth as well as goals of efficiency and profitability. Indeed, in the institutional landscape, differences among the priorities and preferences of business, labour and government help shape locational outcomes.

This chapter is in three main parts. First, the key concepts of corporate strategy and structure and countervailing power are defined and ways in which rival strategies shape locational outcomes are identified. The second part interprets factory location as a strategic bargaining process, specifically with respect to the negotiations between MNCs and host governments regarding new investments and the implications of labour relations for location. The final part briefly comments industrial policy as a social bargain from national and local perspectives.
Organizations, as institutions, are formal structures embedded in society whose behaviour reflects particular rules, tradition and values (Oinas 1995b). Business organizations exhibit a wide variety of forms and pursue a complex range of goals (Ahern 1993a, Heilbroner 1992; Starbuck 1971). As Ahern (1993a) notes, there is one view which emphasizes that organizations seek to use resources efficiently and another which emphasizes that organizations seek to access and control resources. In the context of large firms, growth is usually considered an important goal in itself and one that relates to others, such as executive income, prestige and power (Starbuck 1971). From this perspective, the so-called managerial models of the firm argue that large firms seek a rate of growth which is not too slow, thereby causing financial problems and threats from stockholders and rivals, and not too fast, thereby generating internal problems of coordination, efficiency and planning (Baumol 1959; Marris 1964 and Penrose 1959). In practice, firms can pursue a range of goals. Galbraith (1967), for example, suggests that large corporations seek growth, subject to security and profitability constraints. Of course, plans do go wrong, the economy can change in unexpected ways and firms do restructure and ‘downsize’ in attempts to survive. Yet, among capitalist societies, the desire for growth (‘accumulation’) is deep seated, and the underlying motivations relate to the control, power and prestige that growth and increasing size brings as well as to profits (Heilbroner 1985; Veblen 1932). In large firms, strategic goals are the context in which the location of specific factories occurs.

**Corporate strategy and structure**

Firms grow by implementing strategies (Harrington 1985; Hayter 1976). According to Ansoff (1969), strategies are ultimately driven by the investment decisions of firms and refers to the allocation of resources and selection of policies designed to achieve long run objectives and associated market roles. Thus, the formulation of strategies, whether implicit or explicit, inherently incorporates notions about the actual or anticipated behaviour of other organizations in the environment or economy. In theory, the range of
strategic options for firms is extremely wide. In practice, although by no means invariably so, the formulation of strategy, especially when emphasizing investments in new facilities, tends to reveal 'common threads' with corporate history and established corporate structures.

In theory, individual firms have wide strategic choices. In practice, these choices are constrained by accumulated ‘know-how,’ ‘assets,’ ‘expertise,’ more generally, by 'competitive' or 'entry' advantages with respect to production, marketing, technology, access to raw materials and/or financing (Marris 1964: 113; Caves 1971; Kolde 1972: 178; Langlois and Robertson 1995). Indeed, according to Langlois and Robertson (1995), at the core of each firm's competitive advantage is some (precise) idiosyncratic or firm-specific knowledge that is not shared with other firms. Specific strategies seek to extend the firm's accumulated advantages of know-how, resources and skills, as well as sources of power and size. Occasionally, firms may wish to diversify away from established markets if those markets are in decline. Such diversification, however, is best achieved by acquisition and joint venture.

Types of corporate strategy - There are several classification schemes of corporate strategy. The best known scheme emphasizes the industrial direction of growth in relation to existing activities of firms (Figure 7.1).
According to this scheme, corporate strategies refer to (backward and forward) vertical integration (expansion to internalize inputs and markets respectively), horizontal integration (expansion of existing products to increase market penetration) and horizontal diversification (entry into new products for the same markets). Ansoff (1969: 115-18) also distinguishes concentric growth (diversification of product mix to serve new markets) and conglomerate growth (simultaneously diversification of products, markets and technology). Each of these strategies is further distinguished in terms of 'internal' and 'external' growth. The former refers to investment in new plant and equipment and the latter to the acquisition of existing plant and equipment. Traditionally, strategies of horizontal and vertical integration have been, and remain, particularly important and have featured both internal and external growth. Conglomerate growth strategies, which became important in the 1960s, for the most part involve external growth. Subsidiary companies within conglomerates, however, typically pursue horizontal and vertical integration strategies. Moreover, since the early 1990s, the rationale of the conglomerate, the ability to achieve a superior financial performance by moving funds from declining to growing businesses rapidly, has been questioned even by the conglomerates themselves and several have chosen to spin-off their empires into more specialized parts.
There are other ways of classifying corporate strategy (Freeman 1982; Rumelt 1977). Freeman (1982), for example, distinguishes strategy in terms of technological innovativeness, specifically offensive, defensive, imitative, dependent and traditional strategies. Thus technologically offensive firms are on the leading edge of industrial R&D in order to remain the leading product innovators while defensive firms also invest in very large scale R&D in an effort to 'catch-up' with the leaders. Strategies of technological imitation involve firms in copying the successful technology developed by others while dependent firms simply purchase 'off the shelf' or lease mature technology with perhaps some modest adaptation for local circumstances. Traditional firms rely on technology that has not changed for at least one Kondratieff cycle. Clearly, the classifications of corporate strategies by the nature of industrial integration and technological innovativeness, as well as in other respects, are not mutually exclusive.

The corporate structure follows strategy thesis - In general terms, the deployment of corporate physical and human assets among its various manufacturing plants and offices and the manner in which these operations are integrated and governed defines corporate structure (Caves 1982). In practice, corporate strategies are closely intertwined with corporate structures (Caves 1982; Chandler 1963). Strategies emerge from structures and in turn modify them. Chandler (1963) argued, on the basis of American experience, that corporate structures are adapted following the implementation of corporate strategies (Figure 7.2). According to Chandler's 'structure follows strategy' thesis, US-based corporations such as Ford, implemented strategies which created larger scale and more complex operations which in turn required changes in the structures of command and communication.
In an idealized form, as (some) firms grow, entrepreneurial functions are decentralized and bureaucratized as individual entrepreneurs are progressively replaced by groups of specialized managers; groups of specialized managers with supporting departments; divisions based on functions (such as accounting, production, marketing and personal); divisions based on functions and product lines; and divisions based on functions, product lines and geographic spheres of operation. Indeed, in the US, particular emphasis has been placed on a hierarchical, ‘multi-divisional’ or ‘M’ form of organization. In tandem with the decentralization of decision making functions firms develop new ways of integrating and coordinating increasingly dispersed and diversified operations. From this perspective, integration relates to the organization of information flows within the firm, the insertion of checks and balances on local autonomy and the maintenance of some form of centralized responsibilities. Even in highly decentralized companies, budget control and investment planning, long range R&D and an information flow system that has its ultimate apex in the parent's head-office, provide ways to coordinate operations.
In large firms such as MNCs, decisions as to strategy and structure are the responsibility of technostructures. While typically characterized by strong senses of hierarchy and loyalty, technostructures are bureaucracies in which 'coalitions of interest groups' holding differing views on strategy and structure can occur, even if such differences are rarely reported (Krumme 1981; Soyez 1988a and 1991). The most significant division of interests within the firm is that between management and labour, whether the latter is unionized or not. In a union firm, these differences are formalized and subject to explicit negotiation under sets of rules to which both parties may contribute. Moreover, unions exist within the firm and are part of the firm's environment to the extent that a particular union or union local is affiliated to a bigger union or simply loosely related to a wider union movement.

**Economic landscapes as countervailing powers**

In a neoclassical landscape populated by numerous small firms, economic behaviour is regulated by competitive forces comprising arms length and independent relationships which can be readily substituted for one or another. Indeed, in a perfectly competitive world, the ‘invisible hand’ is a metaphor for the (apparently free) self regulation of markets. While some markets work in this way, in landscapes of countervailing powers big business dominates and their behaviour is interdependent rather than independent (Galbraith 1952, 1967). Indeed, reaction to, and anticipation of, rival behaviour constitutes one form of 'countervailing power' which constrains the autonomy of any one giant firm (Fellner 1944). In this landscape, the critical features of corporate interdependence from a long run perspective are investment decisions, particularly those incorporating product and process innovation, rather than simply price (Schumpeter 1942). Thus, in countervailing landscapes dominated by a few big firms concerned with size, market share, security and growth, strategies implemented by one firm, which feature
product innovations which undermine existing products and investments designed to access new markets or resources, inevitably draw reactions from rivals.

Figure 7.3
Landscapes of Countervailing Power

(a) Competition: the locational overlap model

(b) Competition: the exchange of threats model

(c) Collusion: the spatial monopol model

Oligopolistic rivalry: locational hypotheses - Within oligopolies, interdependent corporate investment strategies can range from competitive to collusive, different types of strategy creating different types of countervailing landscape morphologies (Watts 1978; 1980a). In a competitive situation, for example, equally large rivals may be encouraged to
Pursue locationally overlapping branch plant investments in order to gain a share of each market or a share of a particular natural resource (Figure 7.3a). Vernon (1985: 67-70; 1971) interprets such behaviour as responses to risk and uncertainty as firms who do not match the locational initiatives of rivals potentially forfeit sales and profits in new markets (or potential forfeit access to low cost resources in new supply areas). A number of studies in the resource and especially the secondary manufacturing industries have demonstrated that corporate investment strategies move in a geographically parallel manner (Vernon 1971; Knickerbocker 1973; Rees 1978; Laulajainen 1982; Gwynne 1979). In the petroleum industry, for example, the leading UK and US oil companies collectively invested in the Gulf of Mexico region in the 1930s and in the 1950s and 1960s in the Persian Gulf region (Vernon 1985: 69). In secondary manufacturing, investments by large corporate tire manufacturers (Gwynne 1979) and by leading auto manufacturers (Baranson 1969; Jenkins 1977) in various developing countries also contributed to overlapping facilities, in some cases establishing capacity far in excess of local demand.

In countries with relatively small markets, including advanced countries, this form of competition can encourage an inefficient industrial structure if no individual plant can reach minimum optimal scale. In Canada, particularly before trade barriers started to decline in the mid-1960s, US corporations in several industries established branch plants which served the Canadian market with a wide range of the parent companies' product-mix. As a result of low volume product volumes, however, product-level economies of scale were frequently not realized contributing to what is known as the 'miniature replica' effect (Britton and Gilmour 1978: 93).

A modification of the 'locational overlap' hypothesis, is provided by the so-called 'exchange of threats' thesis (Vernon 1985: 70). This idea is based on the observation that firms in the same industries but based in different core countries establish branch plants in the other country (Figure 7.3b). For example, US-based firms that established branch
plants in Europe were often in similar industries to the European-based firms in the US (Hymer and Rowthorn 1970: 80-2). According to the exchange of threats thesis this behaviour occurs because the leading firms in both countries, threatened by the establishment of foreign owned branch plants in their home market, respond by establishing branch plants in the invading firms' markets. This cross-investment constitutes a 'warning' to invading firms that strong competition in foreign markets will be countered by similar efforts in the home markets of invaders. In still other cases, for example in the American sugar beet industry at the turn of the century (Eichner 1989) and the British brewing industry in the 1960s (Watts 1980b), powerful firms have been able to 'block' rivals from entering a region and competing for sources of supply or markets.

Spatial forms of collusion - Collusion creates different landscapes. Although many forms of collusion are illegal, and not easy to identify, collusive behaviour has exerted important impacts on industry evolution and probably continues to be important (Watts 1987: 123). Collusion may take the form of shared participation in which supposed rivals agree to invest in a region only if they do so together. According to the 'red-line' agreement of 1928, for example, the world's leading oil companies agreed (for over a decade) not to undertake any new developments in the indicated territories, principally in the Middle East, except in partnership with the others (Vernon 1985: 69). The most obvious examples of spatial collusion, however, occur when firms agree to carve up markets (or resources) among themselves to create market cartels and regional monopolies (Figure 7.3c). The evolution of the electrical industry, following the discovery of the light bulb in 1879 and until the 1940s, is an example of how the dominant firms in the US, notably General Electric, and Europe, notably AEG of Germany, literally carved up the global market, on the basis of cross licensing agreements, patent pooling and joint ventures, into "exclusive territories, non-exclusive territories and territories excluded from the agreements" (Newfarmer and Topic 1982: 38). These agreements not only
stipulated where products could be sold but also at what price and where they were to be manufactured. Watts (1980a) cites another example from the UK sugar beet industry in the 1920s of a collusive agreement which divided up supply areas and which directly influenced the location of factories. Thus, the two rivals which had been located close to another and involved in disputes over stealing each other's supplies agreed to build new plants no closer than 30 miles (48 kilometres) to each other (Watts 1980a: 301).

In landscapes of countervailing power, the price (as well as investment) behaviour of firms may be interdependent and organized by or within dominant companies in various ways (Figure 7.4).
Under basing point pricing, for example, the prices charged a customer are the price of the good at the designated basing point plus transportation charges from the basing point regardless of where the good is actually produced (Figure 7.4a). The result is that markets distant from the basing point and served by local producers are discriminated against to the extent that 'phantom freight charges' are incurred. The advantages of such schemes
for producers are that they are easy to administer, provide protection to basing points and potentially create windfall profits. In the US, basing point pricing, such as the Pittsburgh Plus system in the iron and steel industry, were once widespread at the beginning of the 20th century although they have since judged an illegal practice which unfairly discriminates against consumers (Machlup 1947). In Europe, however, basing point pricing is still prevalent and officially sanctioned in several industries throughout the European Community. In terms of the location of new factories, basing point pricing systems typically reinforce existing locations for both producers and consumers. Basing point producers are never at a price disadvantage throughout the market area while consumers can only guarantee not paying phantom freight by locating at the basing point.

Even if illegal, there is the possibility that producers will secretly collude to fix prices in particular markets (Figure 7.4b). It is difficult to generalize the locational effects of such price fixing although a tendency towards encouraging concentration is likely.

Significant levels of transactions in contemporary economies, involving services and goods, occur within large corporations (Figure 7.4c). These transactions are clearly not voluntary, independent or determined by the activities of many competing buyers and sellers, the central characteristics of perfectly competitive markets. Rather, the prices charged by affiliated companies are 'administered' and subject to the policies of particular corporations. Within the internal flow of goods and services, large firms have some discretion as to pricing and this discretion can have important implications for location. For example, oil rich resource peripheries have often complained that the international oil firms deliberately kept the price of crude oil low to reduce ad valorem taxes at the source of supply. In turn, low prices (and ad valorem taxes) shift the location advantage for new refineries towards markets. More generally, large firms enjoy similar discretion over the prices charged to subsidiaries for head-office, R&D and related services.
Governments, labour and other sources of countervailing power - Corporate power is not only constrained by rivals but by the strategies and structures of governments, labour, other organizations such as consumer groups and, most notably in recent decades, by environmental groups, as well as by society's values and customs. There is a marxist view which emphasizes the subjugation of government to the interests of business. In Bradbury's (1980) theory of the state, for example, the function of government is to legitimate capital and provide the necessary infrastructure for capital to effectively exploit labour. From this perspective, the notion of countervailing power is irrelevant. Of course, it is to be expected that governments in capitalist societies would promote capitalism and for corporations to seek to further their own interests, including by influencing government policy. Given these expectations, an alternative 'pluralistic' view of the state permits governments to both support and regulate business and to mediate among a wider range of social interests. Thus, in addition to providing services, incentives and infrastructure for business, government legislation also regulates business in terms of employment, safety, pension and environmental standards, as well as the conditions of competition, and through a plethora of taxes to provide public goods and services.

The most general point to be made about governments in relation to business is that policies, attitudes and forms of mediation vary from one jurisdiction to another. Such variations exist at international scales, for example related to different polices towards foreign investment (Laxer 1991), and at regional scales as reflected, for example, in different business climate measures and commitment to boosterism (Cox and Mair 1988, 1991; Weinstein and Firestone 1978). A similar general point can be made about labour. Thus, at international and national scales there are significant geographies of labour power. Management-labour relations, for example, have evolved on different lines in the UK, Japan and Germany and, even if union power in the UK (and the US) has declined and become less adversarial, unions in these countries constitute different kinds of
countervailing power to business. Within countries, variations in labour power are reflected in the regional distribution of unions (Figure 4.3).

If in the 1960s, countervailing powers principally comprised business, government and labour, in the 1990s numerous 'environmental' groups have emerged to mount increasingly effective campaigns against business behaviour which destroys environmental values. Environmental groups, of varying philosophy, have particularly targeted primary activities such as fishing and mining and the primary manufacturing industries, most notably the forest industries, which are involved in the exploitation of scarce natural resources or are involved in unusually extensive environmental destruction. In recent years, environmentalist opposition to industrialization has occurred for several reasons (Soyez 1995). First, environmental groups have successfully mobilized local coalitions of quite distinct interest groups, such as aboriginal tribes, local tourist operators, fisherman and nature lovers, to oppose industrial development. Second, environmental groups have been successful in 'internationalizing' environmental conflicts over industrial projects, especially by targeting potential opposition among consumers of export oriented projects. Third, some environmental groups have been more willing to take business to court if environmental laws are broken. Fourth, other groups have been willing to break the law themselves to protect environmental values. Finally, and ultimately of most importance, in advanced countries at least, there has been growing social concern over environmental values. In fact, environmental regulations in advanced countries are much stronger and more effective than in poorer countries where it is more difficult, but not impossible, to mount environmental opposition. In any event, geographical variation in environmental regulation of, and opposition to, industrial development exists.

Locational evolution - In landscapes of countervailing powers, evolving patterns of industry are explained in terms of the interaction of long run corporate strategies, government policy and technological change (Britton and Gilmour 1978; Markusen 1987;
Noponen et al 1993). From this perspective, the spatial margins to profitability are shaped by public and private sector policies, rather than simply by 'given' underlying distributions of resources, markets and other location conditions. The particular mix of policies, as well as of location conditions, vary among nations and regions. In the case of Canada, for example, the roots of its particular manufacturing structure originate with the national Policy of the 1870s which established tariffs to protect secondary manufacture and an open door policy to forest investment (Britton and Gilmour 1978). As a result, the tariff encouraged foreign firms to establish branch plants to serve local markets while exports were dominated by the resource industries. Indeed, one of the historically distinctive features of Canada's manufacturing is the high level of foreign ownership (see chapter 15).

CORPORATE STRATEGY: BARGAINING OVER LOCATION

Locational choice occurs as part of investment decisions which have strategic purposes, that is, they are made to meet the basic motivations of corporate strategy (growth, profits and security) by gaining access to new markets or sources of supply in a way that makes sense to individual corporations. Moreover, locational choice is not simply a matter of identifying alternatives, evaluating them and choosing the best, as if the alternatives were all given datum. Rather, technostructures consider alternative bargains, contracts or deals with labour, suppliers and consumers, and discuss options with different and varying levels of governments such matters as infrastructure provision, tariff levels, profit repatriation, taxes, subsidies, zoning, energy supply and environmental impact analyses and regulations. In this regard, the spatial mobility of 'new' capital provides technostructures with a fundamental bargaining advantage in relation to 'local' labour and governments. While labour and governments have geographically fixed planning horizons technostructures do not; new capital has wider location options.
Theoretical frameworks which have explicitly interpreted location as a bargaining process have emphasized either bargains between MNCs and host country governments (Contreras and Gregerson 1975; Goodman 1987; Kobrin 1987) or the nature of labour relations (Clark 1981; 1989). There are also case studies of locational bargaining processes which have examined the roles of firms, governments and labour and which provide the basis for this part of the chapter (Alvstam and Ellegard 1990; Krumme 1981; Soyez 1988a).

**Multinational and nation states**

It is generally argued that during the 20th century MNCs have becoming increasingly powerful in relation to nations and in their ability to influence nation states (Galbraith 1983; Harvey 1982; Peterson 1988). At the regional scale, this observation becomes more emphatic (Krumme 1970). There is debate, however, as to the extent to which this balance in bargaining strength and ability has shifted. Peterson (1988: 159) argues that in the face of a rapidly globalizing world economy, in which productive and especially financial capital have become extremely mobile, nation states have lost their power to manage. A greater weight of opinion suggests that interest groups that are antagonistic towards, or do not entirely share, business values also influence governments who retain considerable powers to regulate their economies (Hirst and Thompson 1992). Hirst and Thompson (1992) also suggest that the majority of large firms that are international in scope remain MNCs, which have distinct 'national' (and regional) 'homes, 'and many fewer that constitute true transnational companies (TNCs) that are state-less with no particular national loyalty. In any event, "Bargaining between firms and nations goes on, spawning business arrangements of varying complexity" (Goodman 1987: 133). One important context in which this bargaining occurs is over direct foreign investment (DFI) when a MNC wishes to build a large new factory in a foreign ('host') country.
According to Kobrin (1987) the bargaining power of MNCs and host country
governments (HCGs) comprises three dimensions: the relative demand by each of the two
organizations for resources which the other controls; the constraints on each organization
that affect the translation of bargaining power into control over outcomes; and bargaining
ability (Figure 7.7). Briefly, the power of MNCs is rooted their technological and
managerial expertise and complexity, their financial resources, international marketing
channels and differentiated products reinforced by powerful advertising campaigns. Their
ability to exercise this power is constrained by competitors who wish to negotiate with
HCGs and by the relative importance of the HC as a market (or resource supplier). The
power of HCGs, on the other hand, is related to the size of domestic markets, resources
and skilled labour pools, the availability of infrastructure and the political situation in the
country especially with respect to stability. This power, in turn, is constrained by high
levels of global corporate concentration, competition from rival countries, existing high
levels of dependence on MNCs and by balance of payments of problems. In addition to
their respective 'power resources' and 'constraints,' the bargaining abilities of MNCs and
HCGs are affected by other factors including past experience in similar projects. That is,
bargaining processes are also learning processes. However, MNCs typically have clearer
and more narrowly focused objectives than HCGs and typically have much better
knowledge of the nature of their activities and can better anticipate the impact of
investments on the local economy (Zurawicki 1979). To an important degree, the
expertise of the MNC is embodied within its international operations and its investment
planning horizons are inherently more global than those of HCGs. Once MNCs have
established factories in HCs, however, bargaining power between MNCs and HCGs can
change (Auty 1993; Korbrin 1987; Vernon 1970). The obsolescing bargain hypothesis,
for example, predicts that over time bargaining advantage shifts towards the HCG as
MNCs can no longer move fixed investments and HCs learn more about the MNC
operations (see chapter 10 for a fuller discussion of this hypothesis).
Bargaining between HCGs and MNCs typically focuses on specific investment proposals. Contreras and Gregersen (1975) and Goodman (1987), for example, analyze the investments of US based MNCs in the forest product industries of Latin America (Figure 7.8).

In their model, bargaining power depends upon the interactions of motivations and 'minimum requirements' as well as resources and constraints. For HCGs, minimum requirements may be expressed as laws or guidelines and for MNCs in terms of internally defined rules. Three types on bargaining situation then arise depending on whether motives are complementary, competitive and conflicting. Conflicts result when minimum requirements are not met over a particular matter. In this regard, key issues often relate to levels of profit repatriation allowed, taxation levels, the location of factories, and the degree to which the proposed factory will export, buy local components, train local workers and hire local management. With respect to location, for example, HCGs
frequently want (for various reasons) foreign investment to be located in 'designated' regions or 'special economic zones.' In many, perhaps most instances, this demand results in a complementary situation since foreign based MNCs may have no particular commitments to any one region and designated areas typically offer the minimum requirements firms need in a location, particularly in relation to infrastructure, labour supply and incentive programmes. In some instances, however, conflict arises and locations have to be negotiated.

*The Icelandic aluminium industry:* - In the planning of foreign investment MNCs and HCGs frequently negotiate locations and specific location factors. Thus, the MNC may seek to 'play-off' one nation, region and community against each to gain a better deal. MNCs can also negotiate location factors in specific places in the absence of any formal comparisons and explicit threats that it will locate elsewhere. Until an investment is made in a particular place, MNCs always have the power of not doing so. In addition, MNCs can argue to HCGs that they have superior knowledge about locational requirements, especially when they represent a new industry to a country. In this context, Skulason (1994) offers an interesting case study of the bargaining processes between MNCs and governments in the establishment of the aluminium industry in Iceland. Globally, the aluminium is highly concentrated and the leading firms are horizontally and vertically integrated. Iceland offered to the aluminium MNCs a low cost power base and tide water access to affiliated sources of bauxite and refining operations in Europe. Alusuisse, a MNC based in Switzerland, built the first aluminium smelter in Iceland in 1969 and the Atlantal-group (a joint venture of three - originally four - MNCs) have negotiated the details of a second smelter, go-ahead decision for which is still pending. The first set of negotiations lasted almost 10 years if completion of the smelter is defined as the end point, or about six years if 'final' approval of the Master Agreement by the Icelandic Parliament and Alusuisse is used. The second set of negotiations began in 1987 and
construction is yet to start although tentative agreement has been reached (Table 7.1a and b).

Table 7.1a

Aluminium Refining in Iceland: The Bargain Between the Government and Alusuisse

<table>
<thead>
<tr>
<th>KEY ELEMENTS</th>
<th>COMMENTS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Location:</td>
<td>ISAL is located in Straumsvík on Reykjanes.</td>
</tr>
<tr>
<td>Power supply:</td>
<td>ISAL is provided with electricity from Búrfell power plant. According to the Agreement price was supposed to be 3.0 mills per KWh the first six years of operation and then drop to 2.5 mills. Actually the price never dropped, instead it kept rising.</td>
</tr>
<tr>
<td>Taxation:</td>
<td>ISAL pays a fixed amount per produced ton of metal. According to the agreement the smelter will pay US$ 12.5 per ton the first six years of operation, then US$ 20 for another nine years and the amount would rise to US$ 35.</td>
</tr>
<tr>
<td>Import duties:</td>
<td>ISAL is exempt from import duties on machinery and raw materials.</td>
</tr>
<tr>
<td>Legal issues:</td>
<td>ISAL is an Icelandic firm, but 100% owned by Alusuisse. Disagreements regarding the Master Agreement will be solved using international court of arbitration, which, however, will use Icelandic laws as guidelines.</td>
</tr>
<tr>
<td>Duration:</td>
<td>The duration of the Agreement is 25 years, but the scope of the Agreement is 45 years as each party has the option to extend the Agreement for 10 years.</td>
</tr>
</tbody>
</table>

Source: Adapted from Skúlason 1994. ISAL is the Iceland Aluminium Co.

Table 7.1b
Aluminium Refining in Iceland: The Proposed Bargain  
Between the Government and Atlantal

KEY ELEMENTS:  COMMENTS:

Location: Keilisnes on Reykjanes.

Power supply: The Proposed smelter will be provided with electricity from Blanda power plant and other yet to be constructed power plants. Price will be a certain percentage of the price of aluminum.

Taxation: The proposed smelter will be taxed pursuant to Icelandic law with some exceptions because of the size and specialization of an aluminum smelter.

Import duties: The proposed smelter is exempt from import duties.

Legal issues: Disputes are supposed to be settled by Icelandic courts pursuing Icelandic laws.

Duration: The agreement is supposed to be 25 years with the firm having the option to extend the contract by two additional five year periods.

Source: Adapted from Skúlason 1994.

Alusuisse's original proposal touched off a contentious debate in Iceland about allowing foreign investment of any kind, but particularly that of a large MNC, into such a small country (of about half a million people). This debate, which constituted part of the context of the entire set of negotiations, was only marginally resolved in Alusuisse's favour and underlines the point that the positions taken by HCGs are themselves compromises and bargains of potentially highly variant views. Nevertheless, negotiations continued because Alusuisse and the Iceland government (if not the opposition parties) had overlapping motives. Alusuisse saw Iceland as a large source of cheap hydro-power
accessible to its European manufacturing base and the government wanted to diversify Iceland's economy by utilizing its water resources.

The negotiations themselves focused on the interrelated questions of location, power supply and cost, scale of plant, taxes, import duties (on the alumina), length of contract and the legal status of the plant. The power supply issue, for example, raised questions as to the number, size and location of new power plant, which in turn depended on the size and location of the smelter, and the price of this power to Alusuisse. At the time, the government entertained some hopes to use the smelter to meet regional development goals, particularly to spread growth away from the capital region of Reykjavik. Of five alternatives considered, however, Alusuisse strongly preferred the Reykjanes (Straumsvik) site, near Reykjavik, which was determined as the low cost option. Since the government's desire to attract the aluminium industry to Iceland was far greater than its concern over location within the country, this location was the one chosen (Figure 7.9). On a legal matter, however, the government was forced into a far more difficult compromise, one which almost scuttled the project. While the government wanted Icelandic law to govern the operations of the smelter Alusuisse insisted on the primacy of international courts of arbitration. The final compromise allows Alusuisse to use international courts, if necessary, but these courts should take into account (in some unspecified way) Icelandic law.
The Atlantal-group has also negotiated an agreement with the Icelandic Government. Much the same sets of issues were involved in this negotiation although in this case location within Iceland involved more controversy. In particular, while the government felt more strongly about promoting regional development within Iceland, Atlantal's smelter will be built adjacent to the existing one if the project goes ahead. Yet Atlantal is not affiliated with Alusuisse and its choice of location seems to have been based on a rather odd cost comparison in which the alternatives considered (Figure 7.9) were required to include expenditures for environmental control while the chosen site was not! The Atlantal group, however, strongly preferred Straumsvik which is close to both the Reyjkavik and international airport thus facilitating access for parent company executives to government decision makers and the proposed smelter. The existing smelter is also proof of the viability of this location. As it happened, the signing of a Master Agreement was delayed in the early 1990s by the Gulf War and because Russia has been trying to obtain hard currency by selling off its aluminium stocks which in turn is driving down prices. If the project once more becomes economically feasible there may of course be some re-consideration of location conditions.

Location as a bargaining strategy with labour
Do firms use location as a bargaining ploy with labour? New capital investment, particularly that by large corporations, is relatively more mobile than labour and by investing in new locations firms can find and develop new kinds of labour bargain while the threat of investment elsewhere can potentially be used to extract concessions from an existing union in an existing factory. Within the geographical literature, early text books (Estall and Buchanan 1980), and numerous locational surveys since the early 1950s, frequently noted concerns by firms regarding labour costs, attitude and unionization (as well as, it might be noted, for skill and availability). For many firms contemplating investment, unions are perceived negatively for their ability to negotiate high wages, non-wage benefits and limits to the scope of managerial autonomy and to organize strikes. On the other hand, firms build factories that are planned in cooperation with unions.

The significance of new locations - It is widely recognized that factories in new locations provide the most favourable opportunities with respect to hiring new labour forces and creating new labour bargains (Barnes, Hayter and Grass 1990; Massey 1984). Once factories are established, existing work practices, attitudes and agreements are difficult to change. Indeed, whether or not labour characteristics are important location factors, the hiring of labour at the start-up of plants have long term impacts. Thus in many primary manufacturing activities, labour costs are a small component of overall costs and labour factors are of little importance in the location of new factories. Even so, new factories provide firms with unique flexibility to hire workers with what they consider to be desirable characteristics. This flexibility is particularly apparent in strongly unionized industries where once a workforce has been hired job mobility along particular lines of progression is constrained by seniority or the hiring date of workers.

New pulp mills built in Canada in the 1970s, including one built in the 'new town' of Mackenzie, British Columbia, for example (Figure 7.5), recruited extensively across
Canada, particularly to obtain experienced, married pulp and paper workers from other small, isolated towns.

The firm deemed that workers with these kinds of characteristics would be more productive and more stable and so invested considerably in its recruitment drive to increase its choice of workers. Once in operation, seniority became a guiding principle of internal employment change so that the start-up of the mill offered the choose employees for positions other than starting positions. Similarly, from the perspective of the workers recruited from established pulp mills, the new mill at Mackenzie offered chances to 'jump' their position in the line of progression or job ladder. Once hired, workers also became 'locked-in' within the vertical line of progression of the Mackenzie mill. It might be noted that another firm which built a pulp mill in a remote British Columbia location at the same time, but which did not invest seriously in worker recruitment, experienced much greater
problems of labour turnover and productivity (Hayter 1979; Ofori-Amoah and Hayter 1989).

In secondary manufacturing activities, the desire for a new labour bargain may itself be an important location factor. The relationship between labour bargains and location is demonstrated by Clark's (1981) re-interpretation of the product cycle model.

Re-interpretation of the product cycle model

Clark’s (1981) re-interpretation of the product cycle model accepts its premise that as products mature firms wish to relocate from urban agglomerations to more rural locations. However, Clark suggests that such filtering down can be interpreted as a labour control strategy as well as, or even rather than, a desire to reduce labour costs. The large state variations in levels of unionization provide a plausible underpinning to this argument (Figure 4.3). Clark begins by recognizing that labour as a location condition is not just a cost component. Rather labour enters into complex contractual negotiations with management which in several countries occur within the framework of collective bargaining. Within such a framework wages, social benefits and how work is to be organized is negotiated (Figure 7.6). These negotiations form what Clark calls “the employment relation” which comprises two main conflicting impulses. First the relation is one of mutual antagonism as management and union each seek to control the production process (in terms of tasks, speed, organization) and the conditions of employment (in terms of hours worked, wages, social benefits). Second, the employment relation is one of interdependence because workers need jobs and firms need labour.
There are laws, such as minimum wage laws, working age, which are nation or region wide, but conditions of employment and control over production process is to some extent negotiable. In these matters management and labour are trying to control each other. Moreover, in Clark's argument, management wants to develop different kinds of bargains with the scientists, engineers and skilled labour associated with research and
development (R&D) and product innovation in the early stages of the product life cycle than with the relatively unskilled workers employed in the mature stages of the product cycle. From this perspective, the maintenance of R&D personnel (and highly skilled workers) in established urban core regions and the dispersal of mature products and unskilled work to rural locations represents a bargaining strategy with labour.

Basically, Clark argues that firms spatially separate these labour groups in order to treat them differently. On the one hand, the firm has professional scientists and engineers who have considerable formal education and firm-specific training, are “mentally and physically agile” and who are "problem solvers" responsible for interesting, complex and uncertain tasks which take considerable time to complete. For the firm, such scientists and engineers are relatively expensive to recruit and expensive to train in the sense of learning how to apply their education and experience to the specific needs of the firm and in relation to other team members. Loss of such employees is costly to the firm because replacement costs are high. Consequently, firms may want to provide extra incentives to these employees to stay with the firm in the form of high wages, good non wage benefits, attractive work conditions, and high levels of stability, even during recessions. Indeed, the preferences of these workers is important to the location of R&D facilities (Table 4.5). Some idea of the importance firms can attach to their in-house R&D groups is revealed by IBM’s decision in the 1970s to take some of its scientists to court who were trying to leave the firm. For IBM these employees were clearly critical to its competitive advantage and to its competitive disadvantage if they should move (Krumme and Hayter 1975: 330).

In contrast, in the mature stages of the product cycle model, firms employ low skilled workers with little formal education and who require limited training to perform boring, repetitive jobs. These workers are relatively easy to recruit and turnover costs to firms are relatively low. Consequently, as Clark notes, firms are more interested in limiting the wage and non wage benefits of unskilled workers and in treating them as true
variable factors of production, hired and fired according to demand conditions. However, in Clark's (1981) view, if different groups of workers are in the same location then the firm's bargaining powers are reduced with respect to the unionized employees. Thus, if in the same location, the union may gain bargaining power by knowledge of benefits received by other groups and, especially through ‘strategies of continuous negotiation’ in which unions place firms under constant pressure to grant concessions, unions may be able to obtain ‘cascading’ benefits within the context of a series of collective bargaining agreements. Clark also suggests that in urban agglomerations unions can focus on the weakest firms to gain concessions and force other firms to follow suite.

Accordingly, in this view, firms derive bargaining advantages, beyond that of hiring lower waged labour, by decentralizing low skilled work to peripheral locations. In particular, the decentralization of unskilled work to rural areas can break the ‘demonstration effect’ in which unions derive goals from benefits achieved by other groups; break the cycle of continuous negotiation and cascading benefits; and re-assert managerial authority over the production process and conditions of employment. Firms may also find that in new locations it is easier to innovate technology as there is no need to negotiate with unions on how such technology will be introduced, which employees will have rights to be retrained and how the new process will be run.

In a large scale of survey of almost 400 branch plants manufacturing mature products and which located in nonmetropolitan areas of the US South, Johnson (1991: 402) did find labour costs and availability to be the two most important local location factors. He agrees with Clark, however, that 'many companies....are less concerned about low wages [or labour availability] specifically than their ability to control the relationship between management and labor.' This same study further emphasized the importance of 'nonlabor factors in understanding the locational behavior of late-stage activities.' Johnson (1991: 406) particularly noted the importance of good trucking connections, a favourable tax environment and an abundance of land. Thus, this study corroborates
Moriarty's (1983) earlier survey of plants locating in North Carolina which found that while a range of labour factors were important, a wide range of other location-specific factors were also relevant (Table 4.X).

More complex bargains

In the context of branch plants manufacturing mature products, bargaining processes are often more complex than anticipated by Clark's (1981) revised product cycle model, and related literature (Sayer and Walker 1989). This model interprets location as a labour control strategy. In practice, the motivations and forms of labour bargains are more varied. For example, firms may wish to establish labour bargains which enhance worker responsibility and participation in work organization and which reflects the needs of the workforce rather than established management traditions. Moreover, new locations can involve firms in bargains with governments, suppliers, consumers and other organizations. In addition, for multi-plant firms, the bargains struck at new locations may still be in some way affected by its bargains at existing locations. An example of a relatively complex bargain, which featured arguably the most radical labour relations experiment of recent decades, is provided by Volvo's new, albeit short-lived plant at Uddevalla.

Volvo's Uddevalla experiment - In the mid-1980s, Volvo decided to embark on a horizontal integration strategy in Sweden and build new, integrated auto assembly capacity and to restructure its labour relations. In Sweden, Volvo's main existing facilities are at Torslanda, west of Gothenburg, where an assembly plant is integrated with a body shop and paint shop (Figure 7.7).
This plant was opened in 1964 and another assembly plant was opened in Kalmar in south-eastern Sweden in the early 1970s. Both these locations are supplied from other Volvo plants including Skövde (engines) and Köping (transmissions), as well as from a large number of subcontractors (Fredriksson and Lindmark 1979). As Alvstam and Ellegard (1990: 188) note, a new body shop, paint shop and assembly operation could have logically been added to the Kalmar site, at that time only an assembly operation, or at Olofström which had a press shop. In either case, new integrated facilities would have increased the efficiency of existing flows of components and processes within the Volvo system.

In practice, Volvo eschewed its Kalmar and Olofström options in favour of a new location, specifically Uddevalla to the north of Gothenburg (Figure 7.7). Several key factors underlay this choice, notably availability of skilled labour, government incentives and reasonable accessibility to Volvo's existing operations. In addition, Volvo desired "to develop new ideas of work organization" which it perceived could be most effectively accomplished at a new site (Alvstam and Ellegard 1990: 189). There were several, critical
sets of negotiations involved in the establishment of the Uddevalla factory which opened in 1988. First, Volvo sought the union's cooperation to develop a radical, more humanistic form of work organization. Volvo's motives behind the creation of more interesting, varied and responsible work experiences was to offset the problems of increasing rates of turnover and accident rates associated with short cycle repetitive work, and to offer jobs acceptable to better educated Swedish youth, a declining cohort in the Swedish population (Berggren and Rehder 1992: 195). While more details of the new work practices are provided in chapter 11, it might be noted the new forms of work organization, based around the idea of entire cars being assembled by small teams of around 10 workers, took management and labour several years to develop and several plans were discarded before the final one was accepted (Alvstam and Ellegard 1990). This form of labour bargain is entirely different from that anticipated by labour control models.

A second set of negotiations occurred between Volvo and the Swedish (and local) government (Alvstam and Ellegard 1990: 190-2). After the mid-1970s, the Swedish shipbuilding industry declined rapidly and the government took over the shipyards and responsibilities for finding jobs for former shipbuilding workers. While Gothenburg's economy grew sufficiently to compensate for lost shipbuilding jobs at Uddevalla closure of the shipyard threatened significant problems for the small community of 45,000 people. Consequently, the government offered substantial incentives to firms locating in Uddevalla and improved highway connections to Gothenburg. Volvo was able to take advantage of these incentives and even negotiate additional ones related to financing, cash grants and tax deductions based on the accumulated losses of the former shipyard which Volvo had acquired. (Interestingly, on the basis of this bargain, SAAB, Volvo's Swedish rival, convinced the Swedish government to grant it similar concessions; Alvstam and Ellegard 1990: 206). However, and bearing in mind the region has been hit by acid rain problems, Volvo was unable to convince provincial authorities to grant it a license to emit
1,700 tons of solvents annually into the air. Volvo then decided against a paint shop and Uddevalla was established only as an assembly operation.

Third, another set of negotiations involved Volvo's internal politics. As noted, Uddevalla was chosen from among alternatives based at Volvo's existing operations and there are suggestions that the Uddevalla experiment in labour relations was not entirely accepted throughout Volvo management and that as Volvo's markets became increasingly sluggish, vested union interests were not interested in preserving Uddevalla at the expense of Gothenburg. Moreover, the Uddevalla plant was allocated the responsibilities to produce older Volvo models. Even so, according to Berggren and Rehder (1992), in terms of productivity, quality, cost-effective technical solutions, cost savings related to health, lower tool and training costs and in reducing delivery times to customers, the Uddevalla plant recorded rapid improvement after 1990 which either met or surpassed the performance in the Torslanda plant. In their view, when Volvo rationalized capacity, it was easier to close the newer ('least senior) and small Uddevalla plant than the bigger and older Torslanda plant supported by the power of vested management and union interests.

**Contesting closure** - As de-industrialization gathered momentum, first in the UK then elsewhere, the closure of factories in old, specialized industrial regions the 1970s and 1980s were often contested by workers and communities striving to protect local employment opportunities (Hudson and Sadler 1986). As Hudson and Sadler (1986) note in a European context, anti-closure campaigns, were mounted by workers in several countries in several industries, but most notably in steel (Hudson 1984; Hudson and Sadler 1983; Hudson and Sadler 1989; Sadler 1984). While in some places these campaigns were fought by workers in the specific places threatened by closure, in other places workers formed alliances with local community business interests and were supported by broader, regional worker solidarity. The anti-closure campaigns were especially strong in nationalized industries and where it could be demonstrated that
threatened plants were viable so that proposed closures reflected particular political choices (Hudson and Sadler 1986: 182).

Closures or threat of closure is a potentially, significant bargaining chip for firms trying to convince workers to change the existing employment relation. The problem for unions is that the granting concessions to firms in order to keep a factory open may enhance their vulnerability to further concessions without necessarily eliminating the problem of closure. Such bargaining at existing locations is particularly difficult (chapter 12). Whether or not unions and communities are asked for concessions, factory closures, especially large scale closures in specialized communities, raise questions about the rights of workers and communities that are directly affected (Clark 1991; Watts 1991b). As a minimum, it has been suggested, for example, that advanced notice should be given about closures. Others have suggested that unions and local communities should be formally involved in negotiations over closures to assess underlying motivations and to propose alternatives where appropriate. Jurisdictions, however, vary in laws governing plant closure. In an increasing number of cases, firms, governments and labour cooperate to provide counsel to those laid-off including psychological help, family assistance, and advice on training programmes. In some cases financial assistance is provided. There is no easy way to bargain over closures, however, especially for older workers specialized in skills in declining demand and where employment opportunities are difficult to generate. Moreover, given the widespread occurrence of unemployment, 'migration' as a solution is less easy to justify than in previous times.

**The internationalization of bargaining processes**

For MNCs bargain processes are inherently world-wide to the extent that negotiations at one location are compared to those at others. Increasingly, however, the establishment of foreign factories can lead to bargaining processes involving, management, labour,
governments and other organizations, such as environmental groups, on an international scale. Krumme's (1981) study of Volkswagen’s (VW) decision to establish a factory in the US provides an example of bargaining between VW management and various levels of governments, labour unions and car suppliers was on a trans-Atlantic scale.

Volkswagen's first North American strategy - VW's plant was eventually located in 1976 in Scranton, Pennsylvania and VW’s decision to invest in the US is conventionally explained by market access factors (in terms of location) and the value of the Deutsch mark (in terms of timing). But this decision was by no means inevitable and there was considerable pressure on VW to make other decisions. As Krumme (1981) points out, the bargaining process involved lengthy and contentious negotiations among two federal governments, several state governments and labour unions in Germany and the US while VW also became entangled in discussions and disagreements with potential suppliers, as well as established rivals in the US.

In location terms, VW assessed investment alternatives in different regions of Germany and the US. For VW, pressures within Germany stemmed from the fact that VW is partly owned by private shareholders and partly by the State, notably Lower Saxony (20%) and by the Federal Government (20%). In addition, worker representatives comprised fully one-third of the membership on VW’s ‘Executive Board’ and actively participated in the decision as to whether or not VW should invest in the US. Indeed, VW’s executive board is overtly pluralistic and political which ensured that internal debates within VW are controversial, especially bearing in mind that VW’s plants in Germany were located in ‘development areas.’ As Krumme (1981: 346) notes:

> The fact that both governments and unions were already integral parts of the Board led..to further attempts to expand this foothold by getting ‘their men’ into management - attempts
which...resulted in almost constant personality and ideological clashes with and among members of management. Many concessions had to be made to avoid or postpone further direct participation of political figures in management affairs......During the 1974-75 VW crisis several issues, including the US project, were prime election issues at state and federal levels: indeed, it was the VW recession - unlike any other previous corporate event - that brought many of the conflicts and controversies to the surface. There was blame to be distributed and decisions about capacity reductions to be made - unique opportunities for political intrigue and power play.

The upshot of the exercise of ‘political intrigue and power play’ was that VW decided not to close any of its German plants while its decision to enter the US was significantly delayed until the cost advantages of operating in the US became obvious and VW was threatened with declining market share. In the US, VW also became embroiled in further ‘political intrigue and power play’ games. Responses to VW among American firms, for example, varied. Thus, VW complained that US auto suppliers initially offered components at relatively low prices but as negotiations proceeded prices were raised. In addition, rival US auto manufacturers periodically criticized VW as a government owned company which gave it unfair competitive advantages. Indeed, the US auto manufacturers encouraged a Federal investigation into foreign car makers regarding ‘suspected dumping,’ a non-tariff barrier frequently employed by American industry. In this context, Krumme emphasizes the “intriguing” role played by Congressman John Dent who was both a key backer of the federal investigation into dumping by foreign car companies while actively soliciting VW to invest in Pennsylvania.
In looking at locations in the US, VW enjoyed a favourable bargaining position as a result of the intense competition among states and cities for its investment. One report suggested that all 48 continental states made overtures to VW while Krumme (1981: 350-1) lists the efforts of Tennessee, Mississippi, Arkansas, Ohio and Pennsylvania and those of the cities of Baltimore and Cleveland. In the event, Pennsylvania, which provided a lucrative incentive package to VW, ‘won’ the competition (Table 7.2). Such was the enthusiasm among governments in the US to get the VW investment, the situation was less of a MNC ‘playing off regions’ as regions ‘playing off each other other. VW was apparently able to keep negotiations open with Ohio until the Pennsylvania deal went through. At the same time, in Germany, VW made a deal with Lower Saxony regarding parts supply to the Scranton plant. This plant has since closed and VW has recently built a plant in Mexico.

Table 7.2

The Major Items in Pennsylvania's Incentive Package to Volkswagen

1. A $US40 million loan by the Pennsylvania Industrial Development Authority to the (non-profit) Greater Greensburg Industrial Development Corporation to be used for land and plant purchase and renovation, to be repaid by Volkswagen over 30 years at an interest rate of 1.75 per cent over the first 20 years and 8.5 per cent over the last 10 years. Purchase price paid to Chrysler was reported to be $US28 million. (Chrysler estimated the cost of completing the plant to be about $US100 million.)

2. Highway improvements (through a $US26.9 million bond issue) and a rail spur into the plant (through a $US6.7 million bond issue); both received legislative approval.

3. Originally, 2 large state pension funds for public employees had offered to lend VW $US 135 million over 15 years at 9 per cent interest. The interest rate, however, was slightly higher than had been promised by Pennsylvania as part of its original financing package. Volkswagen eventually accepted only a loan of $US6 million on these conditions (and financed the remainder through the private capital market).
4. Tax concessions were offered. Under a revised plan:
   5 per cent for 2 years after production begins
   50 per cent for another 3 years
   100 per cent thereafter

   According to a county official, the revised plan would give the VW corporation a $6 million tax break over 6 1/2 years.

5. A very 'intense' programme, using federal and other funds, to train workers for employment at the Volkswagen plant. The Wall Street Journal reported (1 June 1976) that 'critics of New Stanton location have asserted that the immediate area lacks the pool of skilled labor offered by other sites, such as the Cleveland area'.

Source: Krumme 1981: 352

Industrial Location Policy as a Bargain

At a national level, institutionalists argue that industrial location policy may be a good social bargain for the country as a whole by promoting regional economic equality and political and social stability. Moreover, in contrast to the neoclassical position, social equality is not necessarily achieved at the expense of economic efficiency (Kuttner 1984). Rather, the use of public funds to promote social well being potentially not only produces a more egalitarian society but a more skilled, informed, healthy and productive one. In addition, from this perspective, so-called externality effects are potentially important considerations.

Thus, regional policy which offers incentives to firms to locate in designated regions may well be a 'good deal' for society if such intervention can generate positive externalities and/or if it can reduce negative externalities (Figure 7.11). In brief, this argument is based on the idea that the deflection of investments in new factories from 'core' to 'peripheral' regions will reduce negative externalities in the core and increase positive externalities in the periphery. The negative externalities, or social costs, in the core relate to inflation, pollution and congestion. The positive externalities, or social
benefits, in the periphery relate to the absorption of unemployed labour within the workforce and fuller use of existing social and economic infrastructure which is available at little or no extra cost - the same infrastructure would have to be built in the fast growing regions. For individual firms, the pattern of social costs and benefits may be of little consequence in why they choose particular locations. A subsidy provides a meaningful incentive for firms to take externalities into account. In addition, regional policies need not necessarily lead to the support of otherwise uneconomical locations since spatial margins of profitability are already broad for many activities.

Moreover, to the extent that regional policy enhances economic equality which in turn leads to greater levels of national and social cohesiveness, national economic efficiency may be further promoted. The alternative - more regional inequality and less political and social cohesiveness - not only reduces demands for goods and services but also potentially creates political fragmentation and conflict. Thus, the economy as a whole may be better off as a result of regional policy.

It needs to be emphasized that the circumstances of the social externality/ regional equity arguments vary among countries and over time. In UK, for example, in the 1960s the social externality/ regional equity arguments reinforced each other to help support a substantial regional policy programme and the delivery of substantial industrial incentives to designated regions. The same can be said for Canada in the 1960s whereas in contemporary Japan the social externality rationale for regional policy encouraging the decentralization of industry away from the massive concentrations of people in the Tokyo and Osaka metropolitan areas is a powerful one. In the 1990s in the UK, however, the economic problems throughout the country have substantially reduced the appeal of the externality argument even if regional political and social equity arguments still exist. In Canada, where the social externally arguments could never be as strong in such a huge country, it is now clear that industrial location policy and other forms of regional development have not achieved political stability and social cohesiveness. Indeed,
Quebec, the most important provincial target for region policy initiatives of all kinds, has never been more likely to separate and to formally create a francophone state in North America. Ironically, as more firms leave Quebec for political reasons, the resulting economic problems continue to justify federal subsidies to Quebec. Clearly, whether or not regional policy is nationally a good bargain is complex and needs to be understood in specific national circumstances.

*Industrial incentives as local bargains* -- As previous chapters have noted, while traditional forms of regional policy in many countries have been eliminated or watered down in recent years regions and communities have themselves remained committed to economic development and in many cases industrial incentives of one sort or another are still offered to firms. The incentives, in the form of grants, tax relief and financing, offered by communities and regions, to firms in return for investment, jobs, income and exports may be considered good or bad bargains. From the latter perspective, for example, there is an argument that community-based industrial incentives operate as a zero sum game in which individual regions and communities compete with one another for a limited supply of mobile investment which in turn can 'play-off' one region against another to bargain for more incentives (Cox and Mair 1988; 1991). In this scenario, one community's gain is another's loss and the former is always susceptible to a better offer from yet another community. The previously mentioned Volkswagen story demonstrates that firms are able to play-off one region against another simply as a result of regional initiatives and desires to compete.

Another view argues that from a local perspective, industrial incentives can be a good bargain. In this view, there are limits to the mobility of firms and in any case there is no reasons why principles of competition should not apply to communities as well as firms. Cannon (1975, 1988) suggests that from a local perspective, the crucial yardsticks by which to assess the local efficacy of industrial incentives are incrementality and
significant benefit, the latter including survivability of assisted plants (see Hayter and Ofori-Amoah 1989). As previously noted, incrementality in this context refers to the effectiveness of incentives in changing the investment preferences of entrepreneurs, most notably by encouraging them to locate in a designated region rather than in some non-designated region (locaional incremenality). Cannon further notes that even if locational behaviour is not changed, incentives can affect the timing, scale and financing of investments (non-incremental incrementality). Of course, incentives may have no effect on entrepreneurial incentives. It might be noted that incrementality effects are hard to assess both *a priori* and *ex post*. The *a priori* problem faces local planners who try to determine whether or not a subsidy is actually needed to convince firm to locate in their community, and if it is what form this should take. In the previously discussed Volkswagen story many states and cities within the US reached the conclusion that incentives were necessary to attract investment but offered differing incentive packages each of which was subject to negotiation. The *ex post* problem faces regional planners who wish to evaluate the extent of the incremental effects generated by past policies. This exercise is difficult since it raises 'counter-factual' arguments concerning what would have happened in the absence of the policy.

The significant benefit criterion recognizes that firms vary significantly in what they offer to communities in terms of levels of employment, the quality of jobs, employment equity, skill development, stability, longevity, local linkages and environmental impacts. VW, for example, offered Scranton substantial significant benefits in terms of the number of jobs created, job quality (for example in terms of wages and training programmes) and through purchases of local components and supplies. Given that significant benefits are subject to bargaining, their determination is judgmental. What is an appropriate target for the extent of local purchases, for example? The EC demands that foreign auto makers purchase 80% of their supplies from within the EC while the US has less stringent local rules. Similarly, what is a reasonable requirement for the longevity
of jobs? There are example so firms who have received incentives and never invested and others who have stayed for maybe a year or two before re-locating elsewhere and presumably such behaviour does not constitute a benefit. VW, on the other hand, lasted about a decade in Scranton, a period that may be long enough to generate long term benefits within the community but also short enough to raise questions about the wisdom of the incentive package. Local development bargains can be extremely difficult to judge.

Conclusion

In different parts of the global economy firms engage in different kinds of bargains with labour and governments (and other organizations) regarding employment, work and other matters. In low wage, low skill locations, basic training and skill formation as well as jobs typically are high priorities. In advanced countries, in addition to jobs, advanced skills and interesting work are important. In some cases, firms directly bargain with unions in accepting responsibility for providing work that is appropriate to local values, income levels and education, that is, for local development. In other cases, firms have little interest in local development *per se* and prefer to scan communities in search of labour, inducements and other deals which they can exploit and adapt to their needs.

In practice firms have varying commitments and obligations to local development. As Oinas (1995a: 177) states:

> In their operations, decision makers in some enterprises tend to be willing to take questions of long-term local development into account in their decision making and in their local political action. In other enterprises, on the other hand, decisions are made in a manner that is favorable to their own particular (short-term) interests.
only, even when those decisions have consequences in their local environments.

Similarly, communities are not passive actors in shaping the commitments of firms. At one extreme, for example, communities can emphasize keeping costs low as a way of attracting industry. On the other hand, communities can strive for more complex bargains in which firms fully participate in the development of local economies. The relationships between local community and firms are complex and need to be understood in terms of the geographical dynamics of firms - the theme of the next part of the book.