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Subsidiary's role of MNE:

An analysis of P&G's case by applying the extended IR framework

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Abstract

In this paper, I first took and extended the integration-responsiveness framework by including a new factor, the importance of the local environment, for the role analyses of MNE (multinational enterprises) subsidiaries. Then, I followed the historical transition in the role of P&G' s Japanese subsidiary applying this extended IR framework and examined the implications for their current business.

1 Introduction

These days, many new developing countries including China and India are on a remarkable rise, and taking business overseas is treated like an almost imperative strategy for the Japanese companies to survive. On the other hand, there are reports of a trend for foreign companies to downscale their Japanese subsidiaries. This paper will examine the case of The Procter & Gamble Co. (hereafter P&G), which is an example of such foreign companies. In view of such trends nowadays, it would be important to ask ourselves again what the role of the Japanese subsidiaries is, and whether it makes business sense for foreign companies to invest in Japan.

In this paper, I will follow the historical transition in the role of the Japanese subsidiary of P&G in order to attempt to analyze the business challenges faced by the foreign-affiliated companies in Japan in recent years, with a view to draw out concrete implications. Specifically, I will take a close look at the implications caused by a reorganization of P&G into a front-back hybrid organization in recent years. The analysis by Galbraith (2009) of several companies which transformed itself into a front-back organization and is doing very good business have lead him to a very positive evaluation of such organizations from the point of view of the headquarters. However, there has not been any proper study on the evaluation of the front-back organizations from the point of view of the subsidiaries. It is hoped that this particular aspect of this study will be of value and contribute to the real understanding of such transformations. It seems highly likely that such study would also be inspirational to the Japanese companies.

There are two reasons that P&G was chosen for the purposes of this study. One reason is that this company seems to offer a representative example for analyzing the transformation in the role of subsidiaries. P&G went through a period of huge business deficits and tough troubled times in its early years following their entry into the Japanese market in 1972. The Japanese consumers were very demanding of the products in the market, and it took a long time before they were willing to accept P&G products developed in the US and brought straight into Japan. However, P&G conducted a thorough research of Japanese consumer needs, vastly improved their products based on the results of such research, geared them just for the Japanese market, and was able to achieve great success. Since then these products were introduced into markets in other countries through the P&G network. Such successful business results were acknowledged, and in 1993, one of the four Technical Centers currently in Asia was opened in Japan. Only a very few foreign companies have been able to achieve high share since the moment they set foot in Japan. The foreign companies entering the Japanese market for the first time are faced with challenging factors such as the very Japan-unique distribution channels and a high level of consumer demand. They could only be successful after a period of trial and error[1].

The second reason why the P&G subsidiary was chosen for this study is because it can be considered as one of the foremost example to adopt the front-back hybrid organization model, which in recent years are being adopted by several multinational firms such as Citibank and Hewlett Packard. In 1999, P&G transformed itself from geographical profit centers to a front-back hybrid organization. A front-back hybrid organization is one where the organizational target is to achieve, at the same time, global integration and local responsiveness. For this reason, the front-end and the back-end each has units with a distinct goal, role and organizational logic.

In the case of P&G, the front-end organization is called MDO (Market Development Organizations) and deals with two kinds of customer response. On one hand, MDO deals with the traditional kinds of subsidiary response which places an emphasis on responding quickly to the local needs and information available in each country. On the other hand, MDO also deals with global retailers such as Wal-mart, which already has quite a widespread global network, and for this reason has created a Global Account Team which can respond to bulk requests. The back-end organization is called GBU (Global Business Units) and is responsible for the areas of product development, buying and manufacturing, creating a brand, and marketing and promotions. This GBU works without being limited by national boundaries, and sets up management units which are geographically most appropriate for each brand or product category from a global point of view. Such an organizational reform cannot be carried out without a major global reallocation of business resources and considerable change in the flow of information and knowledge. At the same time, this must indeed result in the redefinition of the role of overseas subsidiaries. It has been reported that there was a major personnel transfer from Japan to Singapore along with a functional transfer. This means that a major change has occurred in the role of P&G Japan (*Nihon Keizai Shinbun* September 11, 2009).

Next, we will examine the framework of analysis chosen for this study. Many different analysis frameworks have already been developed in order to ascertain the role of overseas subsidiaries. In the 80's, as far as the typology of the subsidiaries is concerned, there were integration-responsiveness grid analysis (Prahalad=Doz 1987; Jarillo=Martinez 1990; Roth=Morrison 1990; Taggart 1998a), coordination-configuration grid analysis (Taggart 1998b; Mogaki 2001), and the differentiation of subsidiaries according to the type of MNE (Bartlett=Ghoshal 1989; Ghoshal=Nohria 1989; Nohria=Ghoshal 1997; Taggart 1997), all of which, along with others, were actively utilized in order to classify the role of subsidiaries from various points of view. In recent years, however, it has been acknowledged that it is almost impossible to evaluate the competency of any specific subsidiary at the level of a subsidiary. This type of analysis is now trying to evaluate at more micro level, where in some cases an individual employee is the object of analysis. Also, from the point of view of the overseas subsidiary being a connecting point of the external market and the internal network, some studies have evolved around the embeddedness of local markets (Forsgren=Pedersen 1998; Andersson=Forsgren 2000; Frost=Birkinshaw=Ensign 2003).

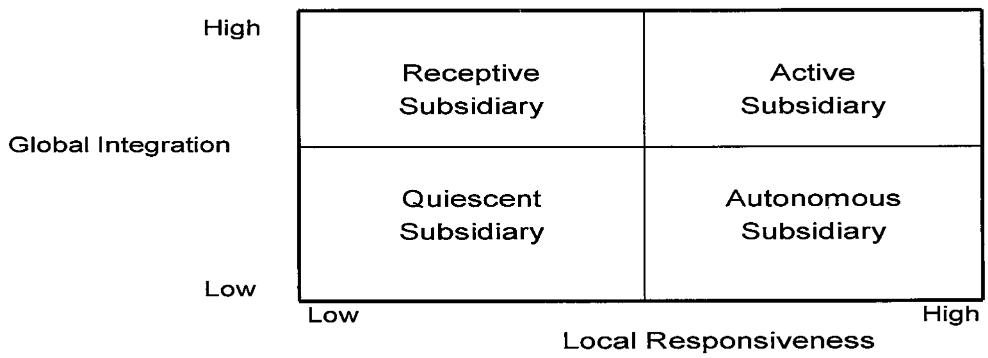
In this study I will apply the integration-responsiveness (I-R) grid analysis as our analytical framework. There are two reasons for choosing this framework. One reason is that, if we follow the shift in the role of the P&G subsidiary since its founding, at each major turning point such as the success brought about by responding to local needs, the establishment of the global technical center, there are elements which directly relates to the explanatory variables used in the I-R grid analysis, and makes it possible to investigate how these changes have affected the role of the subsidiary. Also, by applying the I-R grid over the length of the five periods, I should be able to witness a role change from a dynamic point of view. The second reason for adopting this analytical framework is because the front-back hybrid organization, the organizational structure for Period IV and V of the P&G Japanese subsidiary, is related to the fact that the main reason for creating such an organization was originally to render global integration to be compatible with local responsiveness. As a result of organizational reform, the employees of the Japanese subsidiary was reassigned to MDO and GBU, and the role was by this time no longer that of a subsidiary but that of either GBU or MDO, and a role clarification was necessary in this regard. Since these major organizational changes were conducted so quickly, if the situation is assessed from the point of view of the subsidiaries, they are facing various contradictions and new challenges which have emerged recently. This study hopes to show these changes clearly by analyzing the MDO and GBU in Period V independently on the I-R grid.

This study follows the I-R grid of Jarillo, Martinez and Taggart (see next section for details)as a basic analytical framework. However, in order to reflect the situation of the recent Japanese market in explaining the role of overseas subsidiaries more accurately, I will modify the above-mentioned I-R grid in the following ways as outlined in detail in the next section.

2 Proposing the I-R-E Framework

The I-R grid (figure 1) advocated by Jarillo=Martinez (1990) utilizes the degree of global integration and local responsiveness as the explanatory variable in terms of creating a role classification for subsidiaries. This framework, however, is considered to be insufficient for the purposes of appropriately classifying the role of current Japanese subsidiaries in this study. Consider the role of foreign-affiliated companies in Japan, we can no longer do so without recognizing the effects of rising giant markets of newly developing countries in the Asian neighborhood, such as China and India. This means that the attractiveness, and therefore the importance, of the Japanese market for the foreign companies is comparatively diminished, and thus necessitates transformation of the role of the Japanese subsidiaries[2].

Figure 1 Integration-Responsiveness Framework
Jarillo=Martinez(1990) & Taggart(1998a)

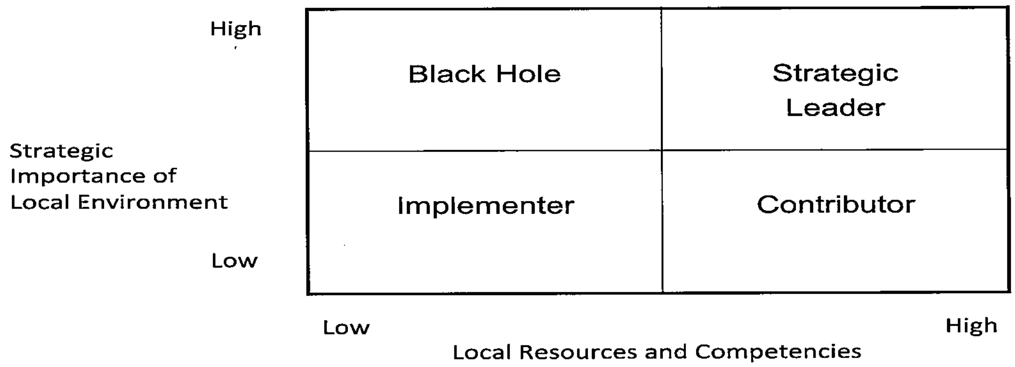


Next let us take a look at transnational organizations advocated by Bartlett=Ghoshal (1989). This model assumes that the factors which restrict the strategic role of overseas subsidiaries are, on the one hand the strategic importance of the local environment and on the other hand the competency of the subsidiaries, as it can be seen in figure 2. If the local environment is very important and the subsidiary is also highly competent, it may become a strategic leader and take on the most important role. If the local environment is not so important for the headquarters, depending on its competency, the subsidiary will be invested with the role of an implementer or a contributor. This study considers it imperative to add on to the framework the importance of the local environment, since the target of this analysis is the foreign-affiliated firms residing in Japan today.

Based on above considerations, I will add a third dimension, namely the importance of local environment to the two explanatory variables of local responsiveness and global integration, thus proposing the I-R-E grid as an analytic framework to evaluate the role of overseas subsidiaries.

(Hereafter, as appropriate, Global Integration will be abbreviated as I, Local Responsiveness will be R, and the Importance of Local Environment abbreviated as E.)

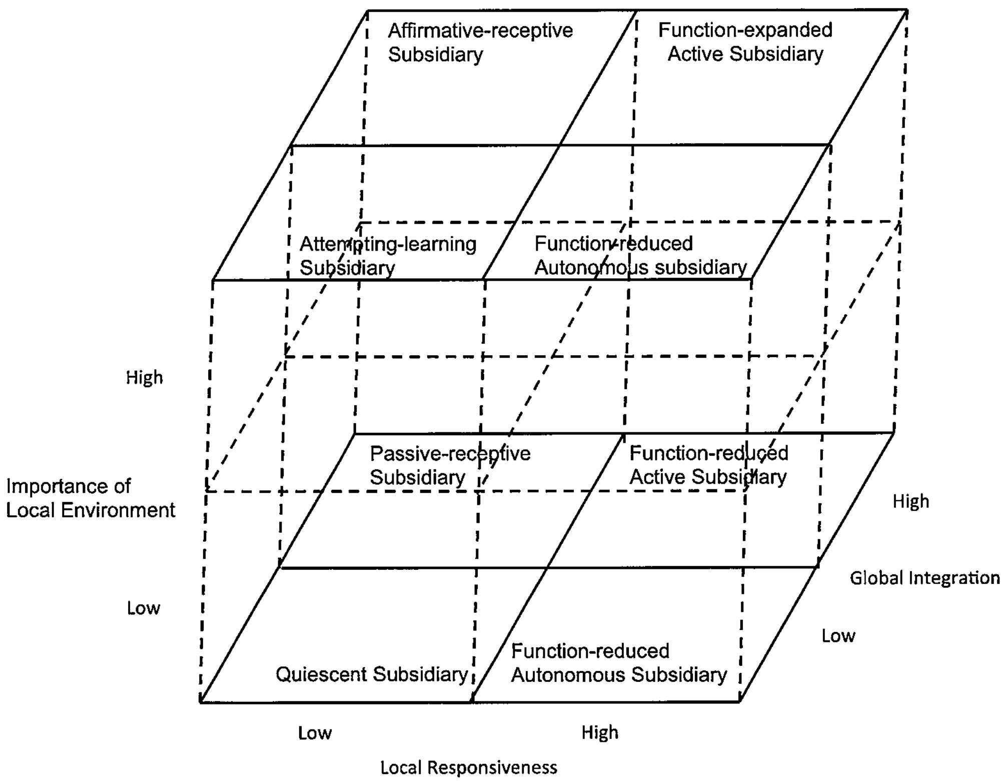
Figure 2 Subsidiary's Role in Transnational Organization
Bartlett=Ghoshal(1989)



When analyzing on the I-R-E grid, the position is determined first by a decision regarding the importance of local environment depending completely on the awareness of the headquarters. The position on the grid is then adjusted by the average levels of integration and responsiveness of various activities in the subsidiary.

Let us summarize the various elements which make up the I, R, and E. The I concerns the degree of global integration in terms of: managing global clients; intra-firm trade of raw materials and half-finished goods; international horizontal division of labor for research and development; and the mutual use of the results of research and development, among others. The R concerns the degree of delegation of decision-making authority to the local subsidiaries, and includes the decision of local sales policies, selection of products for the local market, local development of advertisement and promotion, local modification of manufacturing technology and other activities such as research and development geared toward the local market. Finally, E concerns such factors as the degree of globalization of the consumer; the quality of consumer needs; the size of the local market, the capacity for growth of the local market; the uniqueness of the local market and capacity to learn from it; the competence of the local subsidiary; the possibility of locally utilizing external resources; the level of advancement of local competitors and finally the effect of tax exemption.

Figure 3 Integration-Responsiveness-Environment Framework



As seen in figure 3, the three dimensional matrix using I,R,E categorizes the overseas subsidiaries into 8 types, depending on their role. Each characteristic is summarized in table 1. Active subsidiary as well as autonomous subsidiary, according to the I-R framework, as the importance of local environment decreases, the operations are redistributed and a part of its function will be transferred from the local market concerned to a different region. Therefore, while basically being an active or an autonomous subsidiary, it may shift from being a function-expanded subsidiary to being a function-reduced subsidiary. The two types of function-expanded subsidiaries are comparative to the strategic leader in the Bartlett=Ghoshal model, and the two types of function-reduced subsidiaries are comparative to that of the contributor.

Regarding receptive subsidiaries in the I-R grid, when the clients are globally active and/or the operations require a state-of-the-art technology, then a high level of global integration will be required. In this case, local responsiveness should actually be kept to the minimum. Concrete examples of such

Table 1 Characteristics of Eight Roles of Foreign Subsidiaries

	Allocation of resources	Relationship with HQ or other subsidiaries	Characteristics of the market
Function-expanded active subsidiary	Abundant resources allocated	Information feedback Leadership Role	Expanding market Offers learning opportunities
Function-reduced active subsidiary	Lesser resources allocated	Information feedback Leadership role for specific functions	Matured market
Function-expanded autonomous subsidiary	Abundant resources allocated	Delegation of powers Information feedback	Matured market with specific needs
Function-reduced autonomous subsidiary	Lesser resources allocated	Delegation of powers for specific functions	Matured market with specific needs
Affirmative- receptive subsidiary	Strong and unique firm-specific advantage in the HQ	Centralized coordination	A state-of-art industry such as robots and telecom
Passive-receptive subsidiary	Important resources allocated centrally in the HQ	Centralized coordination	Traditional industry such as consumer goods
Attempting-learning subsidiary	Important resources allocated centrally in the HQ	Gathers local market information Feedback to the HQ	Offers learning opportunities
Quiescent subsidiary	Not much resources allocated	Import products HQ considering withdrawal	Local market considered to be of low importance

subsidiaries can be found in telecom industries or in luxury hotel chains. These cases are categorized as receptive subsidiaries, but the receptiveness shown here is not that of a passive reception where the subsidiary is simply executing all instructions from the headquarters. Rather, they express an affirmative reception in order to maximize the use of global superiority such as a state-of-the-art technology and high brand awareness. Therefore, in figure 3, if the local environment is considered to be very important, the subsidiary would be an affirmative-receptive subsidiary, but when the local environment is not so important, the subsidiary would be a passive-receptive subsidiary.

Finally I will look at the quiescent subsidiary where both integration and local responsiveness are low. However, if the local environment is considered very important, as in the case of the Japanese subsidiary of P&G when it originally entered the Japanese market, it will take on a different role, and become an attempting-learning subsidiary.

According to the classification by Bartlett=Ghoshal, the role of a black hole subsidiary may be comparative to that of an affirmative-receptive subsidiary and/or an attempting-learning subsidiary. The role of the implementer, then, may be comparative to that of the passive-receptive subsidiary.

3 A Shift in the Role of the Japanese Subsidiary of P&G

In this section, I will apply the I-R-E grid to examine the shift in the role of P&G Japanese subsidiary since its entrance into the Japanese market up until the present. I will do this by dividing the time line into five periods. Due to the uniqueness of the Japanese market, business stagnated for P&G when it first entered the Japanese market, but P&G used that period as an opportunity to learn. Since then it increased its local responsiveness which lead it to its success in Japan. Furthermore, since the year 2000, P&G adopted the front-back organization, which was drawing attention as a new form of global organization. However, due to a decrease in the relative importance of the Japanese market, the trend in the recent years is for the functions of the Japanese subsidiaries to be reduced.

Period I (1972-1983) is the period which ended in a great deficit due to failures in the Japanese market operations. Period II (1984-1989), signifying a first step in pulling together the Japanese operations, is the period in which positive results were achieved due to reforms which were initiated on the product itself and method of its distribution. Period III (1990-1998) is the period when the Japanese market was designated as one of the most important strategic markets among the whole of the P&G group. Period IV (1999-2006) lead to the maximum reform of its organization even for the Japanese subsidiary due to the transition into a GBU/MDO organization with a front-back structure. Period V (2007-Present) is the period of large scale reform, of not just the structural changes, but including international personnel transfers.

3-1 Period I Establishing the Japanese Subsidiary (1972-1983)

Procter & Gamble Sunhome Corporation (hereafter P&G Sunhome) was founded in 1972 as a joint venture of P&G, Nihon Sunhome and Itochu Corporation. At that time, Japanese companies were increasing their presence all over the world, and the Western companies were paying attention to their competitiveness. One of the main objectives behind the decision to enter the Japanese market was to learn from the rival manufacturers of Japan as well as to study the Japanese consumers (Dyer, Dalzell and Olegario 2004 pp.213-216).

Basically, the Japanese operations were independent from the headquarters or from other subsidiary companies, and we would have to say that the operations had a low level of global integration. Cheer (synthetic detergent) and Pampers (paper diapers for babies) were introduced by the headquarters. Soap and detergents were manufactured in the factories of the partner company. The paper diaper for babies was a brand new product in the local market, where not even the rival companies had anything like it, and were reliant on imports from P&G group companies overseas. The organization at that time was function-oriented, with the brand management system at the core, just like at the US headquarters. This was not due to a clear intention to globalize the operations, but more an attempt to create a miniature replica of the headquarters, as pointed out by Poynter= White (1985) and often seen in many other US companies at that time.

In terms of adapting to the local market, the decision and choice of brands to be introduced into the Japanese market was made in the US headquarters, showing a low level of responsiveness.

Basically, P&G introduced the US products just as they were into Japan, and attempted to import those US-developed products into Japan using the same product concepts, advertising messages, and methods of promotional campaign. However, the reaction of the Japanese consumers was not good, and the products even failed to gain the support of the wholesalers that they were dealing with[3].

As a result, the company did not do very well, the deficit grew to be quite large, and the possibility of withdrawal was being rumored. However, in the latter half of this period, there was a much stronger awareness of the fact that the Japanese consumers will not accept products which were simply brought in from the US, but alternately, the products which became successful in Japan would be widely accepted in other parts of the world.

3-2 Period II Promoting Local Responsiveness (1984-1989)

The difficulties experienced during the period of P&G Sunhome forced upon P&G headquarters the decision of whether to withdraw from the Japanese market or to make a special effort to pull itself together and to restructure business there. P&G has always denied any consideration of withdrawal. As a public expression of its strong intention to continue its business, it founded a new company in 1984 called Procter and Gamble Far East Inc. Japanese Subsidiary (hereafter P&G Far East), cleared the books of all cumulative deficits, and transferred the projects(Dyer, Dalzell and Olegario 2004 p.219).

During this period, P&G US headquarters concluded a strategic alliance with the rapidly growing Wal-mart group, and carried out various reforms in its distribution structure. In July 1986, P&G Far East also launched on a reform of its distribution channels, and it was at that time that a foreign manager was installed as Head of Sales Department. Up until this time at P&G Far East, foreign managers were positioned in only a few posts, such as the President, Head of Advertising Department, Brand managers, and the Director of Finances. All other posts were occupied by the Japanese managers. It is not difficult to imagine that the news of an appointment of a foreigner as the Head of Sales Department was received with a certain amount of shock by those concerned, since the development of a favorable relationship with the Japanese wholesalers was a matter of urgency during this period. A Special Project team was initiated within the Sales Department which took up the development of a strategy for distribution reform. However, the strategy was formed basically along that of the US distribution reform, as could be ascertained from the appointment of a foreigner as the Head of the Sales Department.

Based on the findings and analysis of this Special Project Team, it was decided to organize a Core Outlet System. Out of the several hundred wholesalers that P&G did business with at that time, 125 core stores were chosen, including several of the most important core wholesalers. The most important core wholesalers were given the exclusive distribution and sales rights to major retailers. In July 1988, P&G applied an open pricing system for Pampers for the first time in Japan. Products were supplied at a price of 5% increase with no rebates, but also with no recommended retail price[4]. In terms of distribution of the products then, there was a slight increase in its global integration.

On the other hand, the company made great progress during this period in terms of local responsiveness. P&G attempted to recover business in Japan and appointed Jager, known for his strong leadership qualities, as President in March 1985. P&G Far East increased its structural unification under Jager, and launched a three-year program "A Great Leap Forward" from July 1985. As part of the program, the organization was streamlined, and the process of product development was reformed. Also, P&G was first among competitors to show consideration for the environment by introducing refill detergent packs and packages produced from recycled paper.

It should be noted that the results of "A Great Leap Forward" program launched in July 1985 helped lead P&G Far East to its turning point. In order to increase its bargaining power vis-à-vis the dealers and to improve its importance as a manufacturer in this market, the program called for rapid introduction of both new and improved products. As a result, sales in Japan shot up from 132 million US dollars to 566 million. The final results of the 1987/88 fiscal year showed a profit, which happened for the very first time since entering the Japanese market. (Dyer, Dalzell and Olegario 2004 pp.223-224). Some of the reasons behind the success of "A Great Leap Forward" program in Japan, were a strong commitment of the US headquarters to make a real effort to pull together business in Japan and the existence of the foreigner with strong leadership as the president[5].

The strategy of local responsiveness was even reflected in the process of product development. For Pampers, the paper diapers for babies, supreme order was to come up with a product significantly superior to that of the Japanese competitors. The period assigned to develop new Pampers in Japan was eight months, greatly shortening its development period in the United States. Based on new Pampers which was improved for the Japanese market, P&G headquarters was able to achieve an advantageous edge against its US competitor Huggies disposable paper diapers manufactured by Kimberly-Clark (Dyer, Dalzell and Olegario 2004 p.235). Yoshiwara (1990 pp.272-273) points out that a Japan local innovation transferred back to the US market resulted in a heretofore unexperienced success, and this brought about a big shift in the role of P&G Far East from being just an overseas subsidiary to an important strategic base for P&G.

Also the case of Whisper sanitary napkin, where sales expanded to national between 1986 and 1988, is known as a trial case of making major responsivenesss in developing a local product based on a global brand. Based on Always which started sales in the United States in 1983, the product was vastly improved down to every detail based on more than 10,000 Japanese women's trial use during a three year period (*Kokusai Syogyo* April 1999 pp.90-91). A TV commercial was developed in collaboration with a major Japanese Advertising Agency Dentsu, but it was for the first time in Japan that a commercial for a sanitary product being on-aired. In spite of the product pricing at a premium, Whisper gained 20% share of the market in its first year of going national. Whisper achieved this by taking share away from Kao and Unicharm which had been the two giants of the market, constantly achieving approximately 40% share together (Suzuki 1996 p.127).

This period saw a great increase in the degree of consolidation and local responsiveness under the leadership of Jager, supported by the approval of and funds from the headquarters. Product development was also strengthened, and the function of this subsidiary in an ever important Japanese market shifted to that of a function-expanded autonomous company.

3-3 Period III Acquiring Strategic Importance (1990-1998)

This period is a period of rapid global integration, not only in terms of Japan-developed products becoming successful abroad, but also in terms of distribution and product development, as outlined below.

Most products sold in Japan were originally developed abroad and then adapted in some ways to meet local needs, but there is also a product known for being developed originally in Japan and then marketed abroad. This product is Max Factor's luxury skin care brand SK-II. P&G officially purchased the Max Factor brand from Revlon in 1991 (*Business Week* April 22, 1991 p.34), but in reality, Max Factor has been manufactured in Shiga factory since 1953 and had already established its position in Japan as a luxury cosmetic. SK-II was developed at Shiga factory, and was sold within Japan since 1980. Since P&G purchased the brand, overseas sales was also accelerated. By the year 2000, sales expanded to include Hong Kong, Malaysia, Singapore, China, South Korea and England, and were introduced since then in Thailand, Indonesia, United States of America and Australia (*Nikkei Bijinesu Asosie* November 1, 2005 pp.104-107).

Several of the brands which were either developed or improved in Japan became a big global success. P&G's strategy is to concentrate its investment on those brands with annual sales of over one billion dollars, and both Pampers and Whisper are billion-dollar brands, and SK-II has grown into brand with sales of half a billion dollars. Following Period II, the brand teams of the locally based Japanese subsidiary continued to take the initiative to design product concepts for the Japanese market and increased their consumer appeal. A high level of local responsiveness was maintained.

In terms of distribution, a step-by-step introduction of the ECR (Efficient Consumer Response) started in 1994. ECR is based on a model built up through the relationship with Wal-mart and is an effort taken up actively by the US headquarters since 1993. ECR aims to maximize the efficiency of various distribution related activities within the organization, with the final goal of providing the consumers with a superior product at a reasonable price. ECR is composed of three elements: (1) SCM (Supply Chain Management), (2) (CRM Customer Relationship Management) and (3) ERP (Enterprises Resources Planning) (*Nikkei Jyouhou Sutorategi* December 1999 p.39).

Regarding SCM, taking headquarters activities as a model, P&G Japan introduced EDLP (Every Day Low Price) in 1996 and BDF (Business Development Fund) in 1997. P&G also decided to join the investors of Puranetto, a joint effort by the local wholesalers and manufacturers to make maximum use of IT[6]. As for CRM, the Sales Department was reorganized from that of geographic divisions to that of divisions by the type of distribution channels. In terms of ERP, business processes were globally integrated in order to cut costs and to maximize efficiency. As a result, the level of global integration increased greatly during this period even in terms of distribution.

As for the importance of the local market, we must say that it was quite high. The Japanese subsidiary raised more than 1 billion dollars in annual sales by 1990, and was considered to be one of the global strategic locations. The accomplishments so far was recognized, and Kobe Technical Center was completed in 1993 where the functions of Whisper product development as well as package developments aimed at the Asia Pacific market, among others, were transferred from other locations. During this period, the level of global integration increased greatly in terms of both product development and distribution reform, and a shift can be seen in terms of the Japanese subsidiary being considered to be a function-expanded autonomous subsidiary to that of a function-expanded active subsidiary.

3-4 Period IV Shifting to A Front-Back Hybrid Organization (1999-2006)

During this period, P&G transformed its organization into a front-back hybrid organization on a global scale (Dyer, Dalzell and Olegario 2004 pp.294-296). At P&G, the front-ends are represented by two kinds of MDO (Market Development Organizations) units, one which is organized on the basis of geography and by country, and the other kind called global account teams, organized for each global retailer. MDO pursues local responsiveness by responding to the needs of the local market. The global account teams support activities of the retailers which pursue scale economy at the global level. In 1988, when a new structure was organized as the Wal-mart team, about 80 P&G employees were stationed at the Wal-mart headquarters in Fayetteville, Arkansas. By 1992, they were called the CBD (Customer Business Development). Currently about 250 P&G employees are stationed, and the teams responsible for a specific country are organized into 10 to 12 person units (Galbraith 2009, pp.168-169). Therefore, it is possible that there is a person responsible for "Japan" among the Global Wal-mart Team, independent of the Japanese subsidiary.

On the other hand, the back-ends are represented by GBU (Global Business Units) organized on the basis of product category units. When GBU were first organized, one unit was formed for each of the following categories, detergents/cleaning products (fabric & home care), cosmetics (beauty), medicine and new projects (health care & new ventures), food and soft drinks (food & beverage), baby products (baby care), menstrual napkins (feminine protection), and tissues/towels, for a total of seven GBU units. Five of the units were stationed at the Cincinnati headquarters, but two of them were stationed overseas. The detergents/cleaning products GBU headquarters was stationed in Brussels, and the feminine protection GBU headquarters was stationed in Kobe Japan.

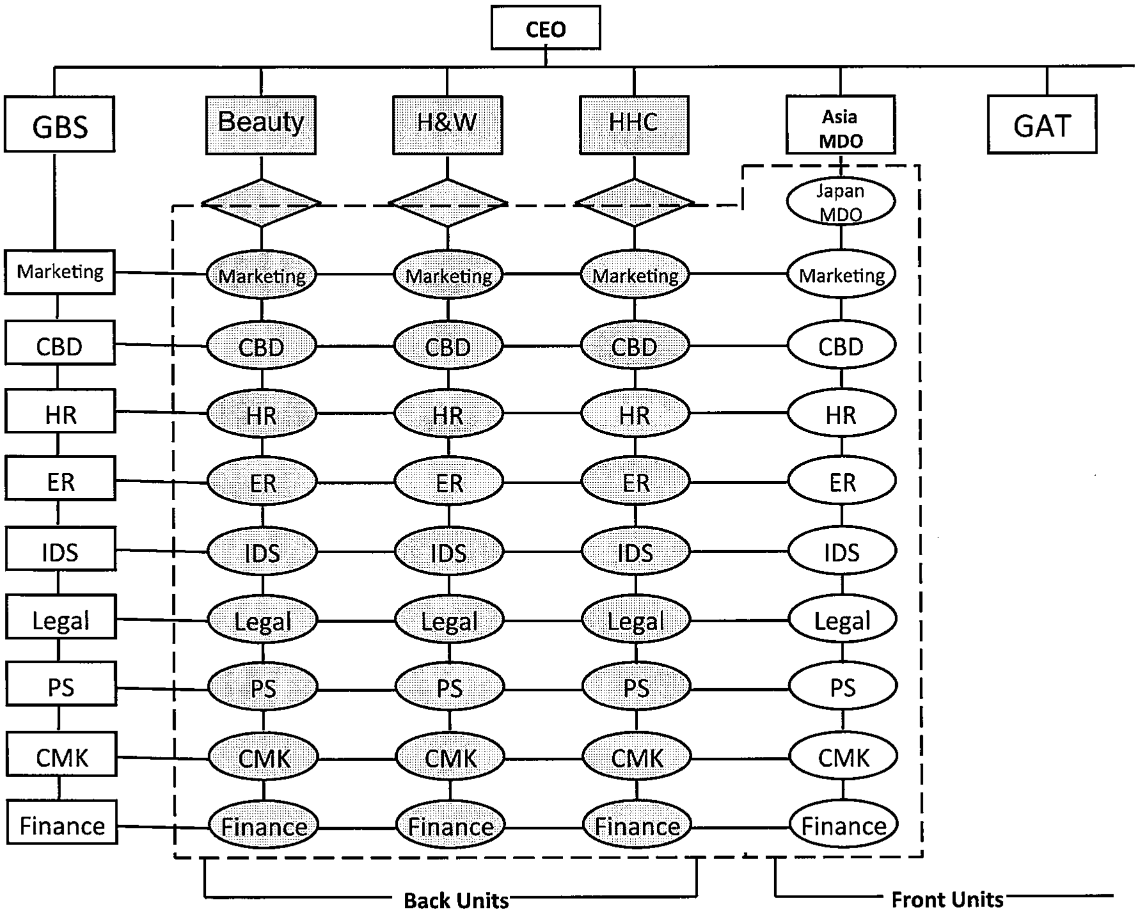
As of 2009, GBU is consolidated into three units, for beauty, for health & well-being, and for household care products. Lafley who was CEO from 2000 to 2009, clarified the respective responsibilities of GBU and MDO in order to further strengthen their relationship (Lafley=Charan 2008 p.35). He believed that it was absolutely necessary for the two teams to respect each other, and for this purpose utilized the concept of "consumer is boss." Specifically, if we are to follow this business philosophy of "consumer is boss," he believed that P&G must concentrate its efforts on two moments of consumer behavior. The first moment occurs in the retail store, when the consumer chooses a product and purchases it, or the first moment of decision (First Moment of Truth: FMOT). On the other hand, the moment when the consumer actually consumes the product, this is the second moment of decision (Second Moment of Truth: SMOT). In this way, the share of responsibility was clarified as in MDO taking responsibility for the FMOT and the GBU taking responsibility for the SMOT. Thus it was made clear that MDO and GBU was considered to have equally important obligations, as opposed to the former brand based structure where the brand teams were held responsible for profit (Ichihashi 2008, p.60).

In terms of legality, Proctor and Gamble Japan Limited (hereafter P&G Japan) was founded as a legal entity in March 2006, and in June of the same year, began to transfer business from P&G Far East [7].

The organization of local operations in Japan under the GBU/MDO structure as a conceptual diagram is shown in figure 4 [8]. The area surrounded by the dotted line indicates the Japanese operation. The oval shapes shaded in gray indicate GBU, and the unshaded ovals indicate MDO. As it can be seen in the diagram, GBU/MDO currently coexist within P&G Japan. Also in figure 4, there are three

Figure 4 Organizing Local Business in Japan under the GBU/MDO Structure

(Conceptual Figure)



diamond shapes located on the boundary (dotted line) of P&G Japan and the rest of the global P&G organization. In real life, these diamond shapes translates to various management levels starting from the brand manager and higher. However, which level of management is located in Japan or not is based on what is most effective for each product category. In some cases the situation is different for each brand within the category, so that there may be someone or no manager at all in P&G Japan to fill the position of these diamond shapes. In reality, from the time P&G entered Japan until Period IV, all brand managers responsible for products sold in Japan actually resided within Japan.

In figure 4, again within the Japan operations (inside the dotted lines) you can see that there are various functions including Marketing, CBD (Customer Business Development), HR (Human Resources), IDS (Information & Decision Solutions), ER (External Relations), Legal, PS (Product

Supply), CMK (Customer Market Knowledge) and Finance. These functions exist equivalently within MDO as well as in each GBU[9]. Within these equivalent functions, an appropriate person is assigned to be responsible for that function, and personnel transfers as well as hiring new employees is also conducted jointly.

As we have seen, at the local Japanese subsidiary where GBU and MDO coexisted, high levels of global integration and local responsiveness was maintained during the Period IV.

First, in terms of global integration, manufacturing as well as R&D technical center were effectively positioned on a global scale. Products were supplied not just by the local factories, but also supported by importing from overseas. In terms of the luxury cosmetic SK-II, for example, Japan is the only global location for both manufacturing and R&D.

Next, in terms of local responsiveness, Japan MDO maintained a high level of local responsiveness, for example, by conducting a joint campaign in collaboration with a large scale supermarket chain as part of its CBD (Customer Business Development). Also within GBU, a brand team was located within Japan at this time, and as a result of continued efforts to respond to the needs of the local consumers in careful detail, they were able to increase their share smoothly[10].

Finally, regarding the importance of the local environment, we must say that a certain level of importance was maintained. First, P&G came up with the policy of Connect and Develop, or activities targeting efficiency by externally procuring about half the newly generated innovations. These activities were unfolded with China, India, Japan, Western Europe, Central and South America, and the United States (Huston=Sakkab 2006) [11].

As one last example which displays the importance of the subsidiary in Japan in Period IV, we should keep in mind that the headquarter of Feminine Protection GBU, one of the first seven GBU, was situated in Japan. This must surely be a sign of the level of importance attached to the Japanese subsidiary, and the work there demanded attention to a high level of global integration. Therefore, to summarize, keeping in mind the shift in the I-R-E grid, we can say that the Japanese subsidiary in its Period IV was able to maintain its role as a function-expanded active subsidiary.

3-5 Period V Promoting Globalization (2007- Present)

As mentioned above, there is a coexistence of GBU and MDO in a local P&G subsidiary. However, beyond 2007 it became increasingly difficult to classify GBU and MDO as one on the I-R-E grid, where the former pursues the merits of global integration, and the latter works to respond locally. The analysis below separates the GBU from the MDO and analyzes the shift on the I-R-E grid.

GBU

During this period, an operational reorganization on a global scale and ensuing international personnel transfer increased rapidly for the GBU acting as a back unit. Six categories of products including hair care products, cosmetics and snacks were transferred out of GBU in Japan to Singapore, which is the strategic center for Japan, Korea and southeast Asia. As a result of this transfer, no more brand manager existed in Japan for some brands. Information from various countries is collected and managed all together in Singapore, enabling it to lead an integrated sales promotion campaigns as well as make decisions regarding the improvement or discontinuation of brands and products (*Nihon Keizai Shinbun* September 11, 2009). For products without a brand management team locally, there is a systematic process whereby the marketing unit within the MDO acts on brand strategy, airing TV commercials as decided upon in Singapore. Such centralizing allocation of management resources and information flow help to increase integration within the area overseen by Singapore.

As for local responsiveness, a decrease cannot be avoided since the brand identity of P&G products sold within Japan cannot be determined locally. However, from the viewpoint of the headquarters, there is logic in transferring a brand management team to Singapore for brands without a serious need for local responsiveness unique to the Japanese market. In other words, the object of "local" used in "local responsiveness" covers an area much bigger and including the Japanese market, and the headquarters believe that the transfer will not decrease the level of responsiveness to the Japanese market [12].

Finally, in terms of the importance of the local environment, all things considered, it is apparent that the Japanese market is becoming relatively less important for P&G. The individual factors contributing to such a situation are; the birth of giant markets in the developing countries such as

China and India; the decrease in the growth rate of the Japanese market; a more widespread acknowledgement that the main battleground for a global rivalry is shifting from being in Japan to being in the developing countries; and the policy of Singapore to offer tax exemptions to foreign investments.

The GBU in Period V shows a high level of integration due to the link with Singapore, but this may in time lead to a decrease in its ability to respond locally in terms of creating a brand or developing a promotion campaign targeting the Japanese consumers. When another factor is added, namely a decrease in the importance of the Japanese market, the role of the GBU will now shift to being a passive receptive unit on the I-R-E Grid.

MDO

Regarding global integration, this is supported by the basic policy of applying the US terms of trade as much as possible. However, as opposed to Period IV, if we are to examine the MDO separately from the GBU which engages in activities with a high level of integration, we may find a decrease in the level of integration during this period.

Next, if we consider local responsiveness, there is a need to respond to the differences in trading customs between Japan and the US, for example, where in Japan the function of the wholesalers are much more important than in the US. In September 2007, a Japanese national was appointed to the highest position in the MDO[13] which was for the first time since it became a wholly-owned subsidiary. Considering this appointment, there is still a possibility of creating a new, balanced and original system of trading which is more adapted to the Japanese market today.

In terms of the importance of the local environment, while acknowledging that the Japanese market is gradually losing its status as the main battleground for global competition in the household goods industry, it is still very important in terms of its comparative market size, its value as a test market for products targeting the global market or the developing Asian countries market, and so it seems that a certain level of importance will continue to exist. However, a relative decrease seems to be unavoidable.

To summarize then, Period V of the MDO will experience a decrease in the level of local responsiveness, integration and the importance of local environment, compared to Period IV, and this will result in a shift in the positioning of the unit from being a function-expanded active unit to a function-reduced active or a function-reduced autonomous unit.

3-6 The Shift in the Role of the Japanese Subsidiary of P&G

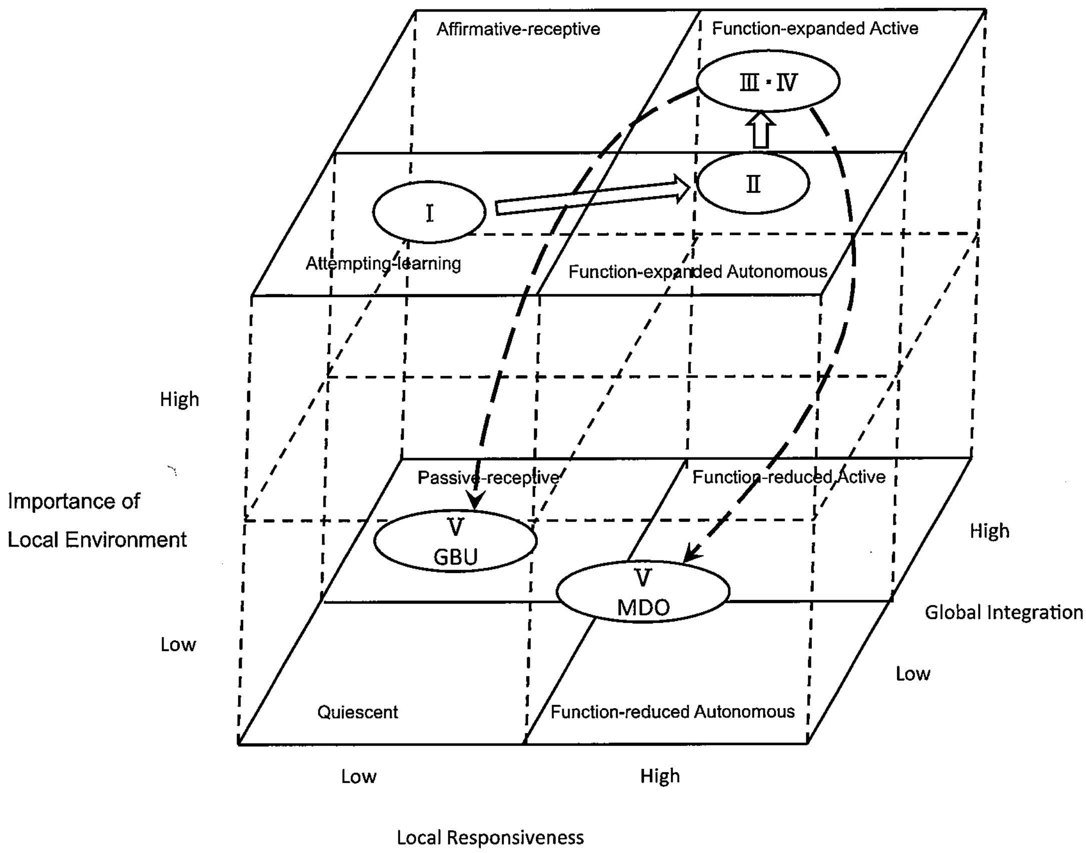
In this paper, the history of the P&G Japanese subsidiary is divided into five periods. In former sections, we looked at the difference in each period of the three elements, global integration, local responsiveness, and the importance of the local environment. In figure 5, I will combine the elements and then see how the P&G Japanese subsidiary role show up on the I-R-E grid and how it shifted through different periods.

To use the I-R-E framework for analysis, first the importance of the local environment is determined from the point of view of the headquarters. The position on the grid is then adjusted by the average levels of integration and responsiveness of various activities in the subsidiary. At least the analysis for Period I through Period IV was conducted in this way. However, in Period V of P&G Japan with its front-back organization, it is no longer appropriate to determine the position on the I-R-E grid in this way. This is because the GBU is in pursuit of I and MDO in pursuit of R so that taking the average of I and R of GBU and MDO as one unit neutralizes the results.

As for GBU, a very high level of global integration is achieved through the allocation and concentration of business resources to those centers for brands or categories not defined by the geographical country boundaries. This resulted in the transformation of the role of GBU in Japan to passive-receptive one and will possibly raise some issues mentioned in the next section.

The function of the MDO is to deal with the customers, and there are two types as mentioned before. One type is the local markets in each country. The other important client is the global retailers. They have expanded sales network across the globe, and have increased their negotiating leverage based on its huge purchasing power. Using these two distribution channels, P&G must deal with the following potential issues, as we will now see in the following section.

Figure 5 Shift in the Role of P&G's Japanese Subsidiary based on the I-R-E Framework



4 Discussion and Implications

MNE have adopted new organizational structures as an experimental trial in order to respond to the uncertainties and the complexity of the current environment (Cantwell, Dunning and Lundan 2010 pp.577-578). We may say that the effectiveness of the front-back hybrid organization of P&G is being tested even today. In the following section, I will examine the operation and challenges of the P&G front-back hybrid organization, a definitely evolving global organization, from the point of view of the Japanese subsidiary.

As far as the benefit is concerned, the first one would be the changes in the organizational structure which transfigured the corporate culture in the Japanese subsidiary. Originally, when P&G Sunhome began its operations as a joint venture with Nihon Sunhome, different kinds of corporate cultures had to coexist within one company, namely, the traditional corporate culture of P&G, where the brand management teams were organized into an elite group, and a corporate culture inherited from the days of Nihon Sunhome where the sales department had a very strong voice. It created a situation where each had difficulties in adapting to one another, resulting in a conflict within the organization. However, when the organization was restructured to become a GBU/MDO structure, the power balance between the two was equalized, and the conflict between the sales department and the brand team was dissolved. This facilitated the effective operation of a rather complicated organization.

The second benefit is from the perspective of career formation. In the former specialist-oriented organization, career formations mainly meant vertical rank promotions. In the front-back hybrid organization, even for a job with an identical function, the choice of horizontal (involving transfers between GBU and MDO) promotions also became available. If we take a look at the organizational structure of the Japanese subsidiary in figure 4, we may get an impression that there are multiple reporting lines, but within P&G Japan, the functional line of orders is always secondary. The merit is more in terms of career flexibility brought about by horizontal personnel transfers[14].

As the third benefit, we can say that there is better coordination between GBU and MDO due to equivalent functions in both.

However, some issues have surfaced. Organizational reforms initiated by the headquarters aim to boost global integration and local responsiveness at the same time. From the current case study of P&G, we found that this kind of reform may result in negatively affecting business at the subsidiary level. We will examine below the challenges and business implications at the subsidiary level.

First, let us take a look at the GBU. GBU positions brand management teams from a global point of view, without being restricted by country boundaries. When business at the GBU was well on track and the reorganization of operations was in earnest, the brand manager post in Japan for SK-II, one of P&G's global brand (500 million brand) was abolished. Considering that this was the first time ever that a brand being sold within Japan did not have a brand manager residing in Japan, and that SK-II was a brand originally developed in Japan, and is totally manufactured within Japan for both the Japanese consumers as well as for overseas sales by using a by-product of Japanese *sake* wine, we can say that this was certainly a revolutionary event accompanying the transformation of P&G into a global organization.

With such an increase in global integration, being transferred overseas becomes a condition for promotion. However, if there is no longer any high level GBU post existing in Japan, then the following three points may be considered a problem.

(1) Difficulty in attracting talented recruits:

P&G Japan has been attracting many talented employees-to-be, as an excellent marketing firm seriously interested in personnel training including training abroad. It may negatively affect this situation if there is no longer a high level position in Japan and therefore it becomes difficult to receive good on-the-job training in Japan.

(2) Lowered motivation for the employees:

A brand manager's main role is to continuously renew and strengthen the brand identity so that the non-existence of a brand manager in Japan may dampen the enthusiasm of developing a brand.

(3) Career Formation:

Nowadays, some Japanese companies have decided to use English as their in-company official language, filling the gap between skills required of personnel in a Japanese company versus a foreign-affiliated one. This may lead one to seek a career path whereby a P&G overseas location is sought as a youth, and then transfer to a (non-P&G) Japanese company in the second half of the career, displaying talents and skills cultivated while working abroad in a foreign company.

As a possible solution to the three points above, an achievement of new creative roles at the subsidiary level will be necessary, in addition to an urgent need for a reform in individual mentality. One of the possibilities of a new creative role is to utilize high level requests expressed in the needs of Japanese consumers to discover ideas for future product differentiations. It may also be possible to position the Japanese market as a lead market for a higher quality products for the whole Asian region.

Next, let us examine some potential issues relating to the consequences of activities by global retailers. Huge retailers of the world possess an ability to procure products at low cost by maximizing scale economies at the global level, and also possess a global distribution and sales network. Via the global retailers' network, such products are supplied to the Japanese market as an imported product. As a result, P&G products that never passed through its Japanese subsidiary could be marketed in Japan. Also such popular brands are traded by independent importers directly with other P&G subsidiaries in an attempt to expand its business with large supermarkets, promoting them as novelty goods. These distributors conduct in-store promotions on their own and expand their sales. Considering the above situation, two problems may be pointed out.

(1) Possibility of cannibalization:

Japan MDO may be selling a product in the same category as the goods which are directly imported from overseas, in which case cannibalization may occur. Presently, fabric softeners which are directly imported from overseas are increasing its share of the Japanese market, but prior to this P&G Japan has been selling and maintaining a high share of the market with a product in the same category but a different brand. It cannot be denied that this situation is certainly a case of cannibalization.

(2) Evalution of P&G Japan achievements:

Until recently, P&G Japan has succeeded in steadily improving and establishing its corporate identity among the Japanese people. If such effort is not appropriately evaluated as being the background to the popularity of the imported P&G products which were never channeled through them, the employees of the Japanese subsidiary may become less motivated.

As a possible solution to the two points above, first, there is an urgent need to construct an evaluation and reward system which will appropriately reflect the accomplishments of Japan MDO which is responsible for all sales in the Japanese market. It may be necessary, for example, to give consideration to the effect of the directly imported P&G brands in the planning of sales estimates, and to identify them or add to it as relevant. This very important issue must be dealt with in order to avoid lowering the motivation of the subsidiary employees.

Secondly, another solution may be to coordinate the negotiations between the P&G global account team and the global retailers, in consultation with Japan MDO, in order to avoid cannibalization of the P&G products in the Japanese market.

As we can see in the example of P&G, the shift in the role of the foreign-affiliated companies evolving from an attempting-learning subsidiary at the initial market entry stage, to a function-expanded autonomous or a function-expanded active one, and then to a passive receptive subsidiary due to the recent decrease in the relative importance of the Japanese market is not considered to be unusual. It has been experienced not only by P&G but also by other foreign-owned firms. The I-R-E framework analysis may be applied to internal units of a subsidiary and not just for the subsidiary as a whole, and is an effective tool to analyze the role and how it shifts in foreign-affiliated firms. Still, how much of the findings in this study regarding the shifts of roles may be generalized is an issue for a future research.

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Notes

1 The difficulty of foreign companies entering the Japanese market is also apparent in the discussions between the United States and Japan, the Structural Impediments Initiative which was started in 1989. This was the very first time that the negotiations seriously considered the difficulties presented by normal Japanese business practice and closed distribution channels.

2 Even for P&G, it was reported that, in 2009, nearly a hundred employees were transferred from its Japanese subsidiary and relocated to Singapore, in order to concentrate various functions there, including product development for Asia and marketing (*Nihon Keizai Shimbun*, September 11, 2009)).

3 The author was an employee of P&G's Japanese subsidiary from 1980 to 1986. The contents of Period I and Period II are based on the author's experience, as well as from Dyer, Dalzell and

Olegario (2004) and various other Japanese documents.

4 Following this action, the price structure which heretofore was considered much more advantageous to the drug store related retailers, became as competitive as the pricing for mass merchandize stores.

5 US headquarters took over Nihon Vicks Company Limited and in May 1988, changed the company name to Procter & Gamble Healthcare Company Limited. Its products greatly contributed to strengthening the Procter & Gamble product line up.

6 In 1999, a minimum unit of order was greatly increased, while at the same time a new system was introduced whereby a discount was offered to any company who satisfied the conditions such as total amount of order or a positive response to EDI.

7 From the fiscal year 2002/2003 (covering the period from July 2002 through June 2003) until fiscal year 2006/2007, P&G Japan achieved a record sales growth every year for five years consecutively, and the sales of P&G Japan in the year 2007 is estimated at 280 billion yen. The reasons behind these successful growths are attributed to the research of consumer needs, the active utilization of research results, value added to the product function which match consumer needs, innovative reform of the relationship with the distribution enterprises, realization of the global scale economy, among others (*Kokusai Shogyo* January 2007 p.22).

8 The contents of Period IV, especially regarding figure 4, is mainly based on interviews.

9 In reality, however, if GBU and MDO found it unnecessary, that particular function may not be staffed.

10 As an example, Febreze is a fabric deodorizing spray which was introduced into the US market in 1997. Technically, this product was developed in the US research facilities, but then its fragrance and packaging was adapted for the Japanese market based on the results of a detailed consumer research (Lafley=Charan 2008 p.276). From October 1998 to March 1999, the sales area was expanded to national, and the result was a big success. In September 2005, an originally shaped packaging of Febreze which made it self-standing, was developed based on the results of consumer research conducted in Japan(*Nikkei Bizinesu* December 26 & January 2, 2005 pp.60-63).

11 One example of this is a sponge product, called Mr. Clean, which cleans without any need for a

detergent. The process of product development started in 2001 when a P&G employee in the position of the Technology Entrepreneur found such a sponge in a variety store in Osaka. Since then this product has grown into a 500 million dollar brand today (Lafley=Charan 2008 p.134).

12 The contents are based on the interview with Ms. Tsujimoto.

13 He is the head of the Japan MDO, simultaneously acting as the President of the Japanese legal entity.

14 In the interviews, the functional lines were explained as being of a "virtual" relationship.

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