This chapter is part of:

The Dynamics of Industrial Location: The Factory, the Firm and the Production System by Roger Hayter, Department of Geography, Simon Fraser University, Burnaby, 2004 (http://www.sfu.ca/geography/people/faculty/Faculty_sites/RogerHayter/books.htm)

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Or Roger Hayter 1997: The Dynamics of Industrial Location: The Factory, the Firm and

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

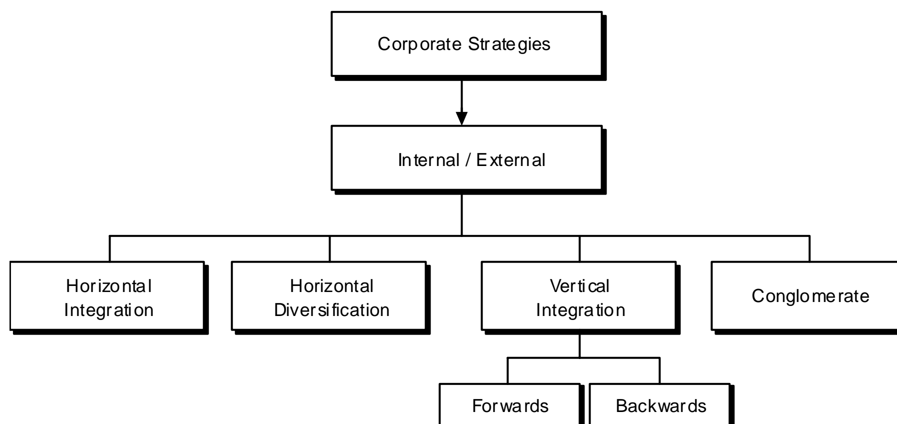
Organizations, as institutions, are formal structures embedded in society whose behaviour reflects particular rules, tradition and values (Oinas 1995b). Business organizations exhibit a wide variety of forms and pursue a complex range of goals (Ahern 1993a, Heilbroner 1992; Starbuck 1971). As Ahern (1993a) 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

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.

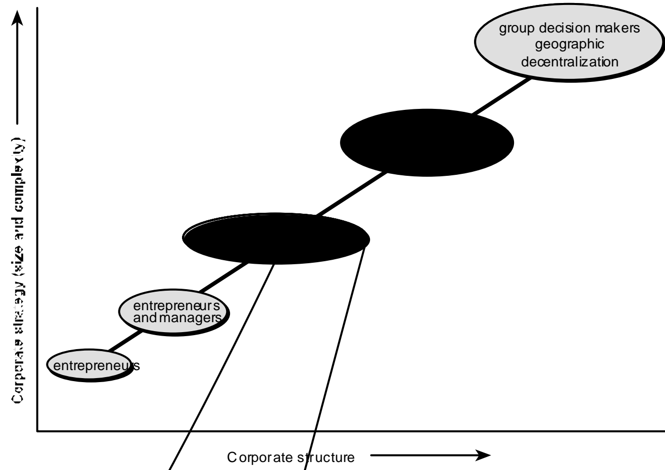
Types of corporate strategy - There are several classification schemes of corporate strategy. The best known scheme emphasizes the industrial direction of growth in relation to existing activities of firms (Figure 7.1).

Figure 7.1
Types of Corporate Strategy



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.

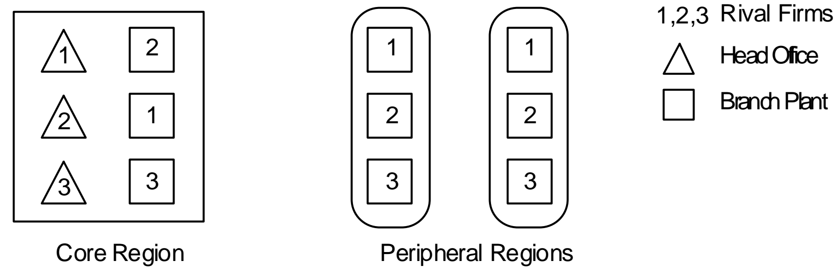
Figure 7.2
The Corporate Structure Follows Strategy Thesis



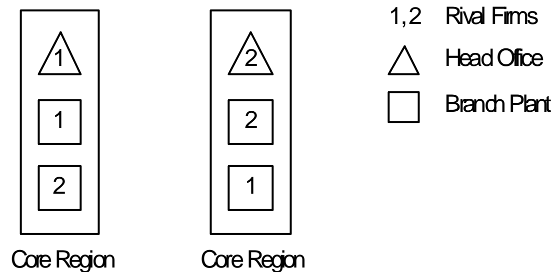
product innovations which undermine existing products and investments designed to access new markets or resources, inevitably draw reactions from rivals.

Figure 7.3
Landscapes of Countervailing Power

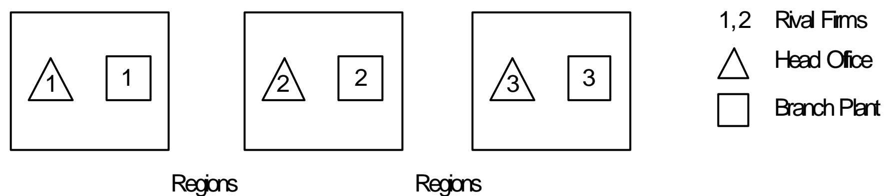
(a) Competition: the locational overlap model



(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

nufactu,have

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).

Figure 7.4
Interdependent Pricing:
Examples of Collusion in Landscapes of Countervailing Powers

(a) The basing point pricing system

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 transaction 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.

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

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

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).

Figure 7.8
Mackenzie British Columbia:
Labour Shed of Pulp Mill at Start-up, 1973

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

KEY ELEMENTS:	COMMENTS:
Location:	ISAL is located in Straumsvík on Reykjanes.
Power supply:	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.
Taxation:	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.
Import duties:	ISAL is exempt from import duties on machinery and raw materials.
Legal issues:	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.
Duration:	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.

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 exly: fBT12 0TJ9 -1pm.ue pm

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

Figure 7.9
The Employment Relation (ER)

E.R. = mutual antagonism + mutual interdependence

control over production process (tasks, speed and organization of work)

conditions of employment (hours worked, wages, benefits)

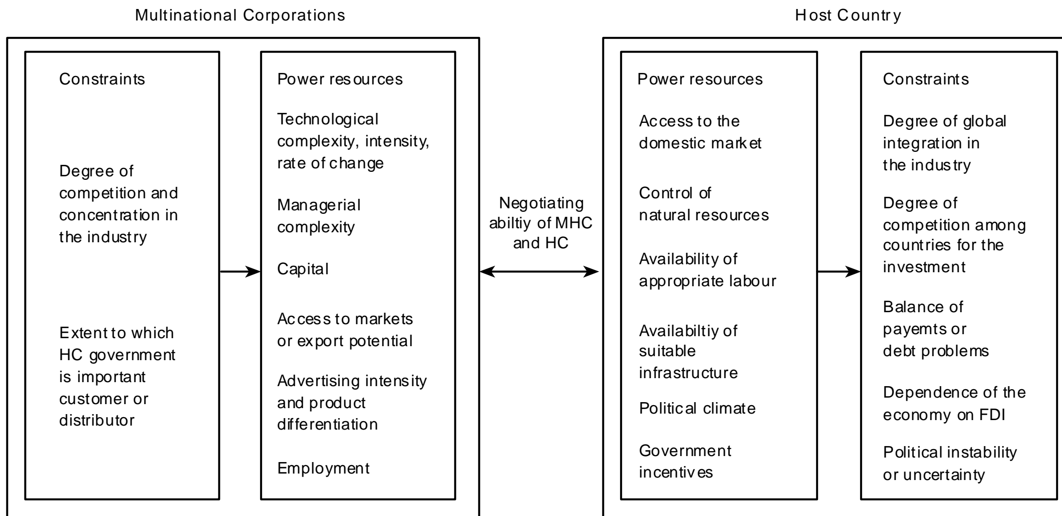
workers need jobs
firms need labour

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 oks

Canada, particularly to obtain experienced, married pulp and paper workers from other small, isolated towns.

Figure 7.5

Components of the Bargaining Relationship between MNC and HC



problems of labour turnover and productivity (Hayter 1979; Ofori-Amoah and Hayter 1989).

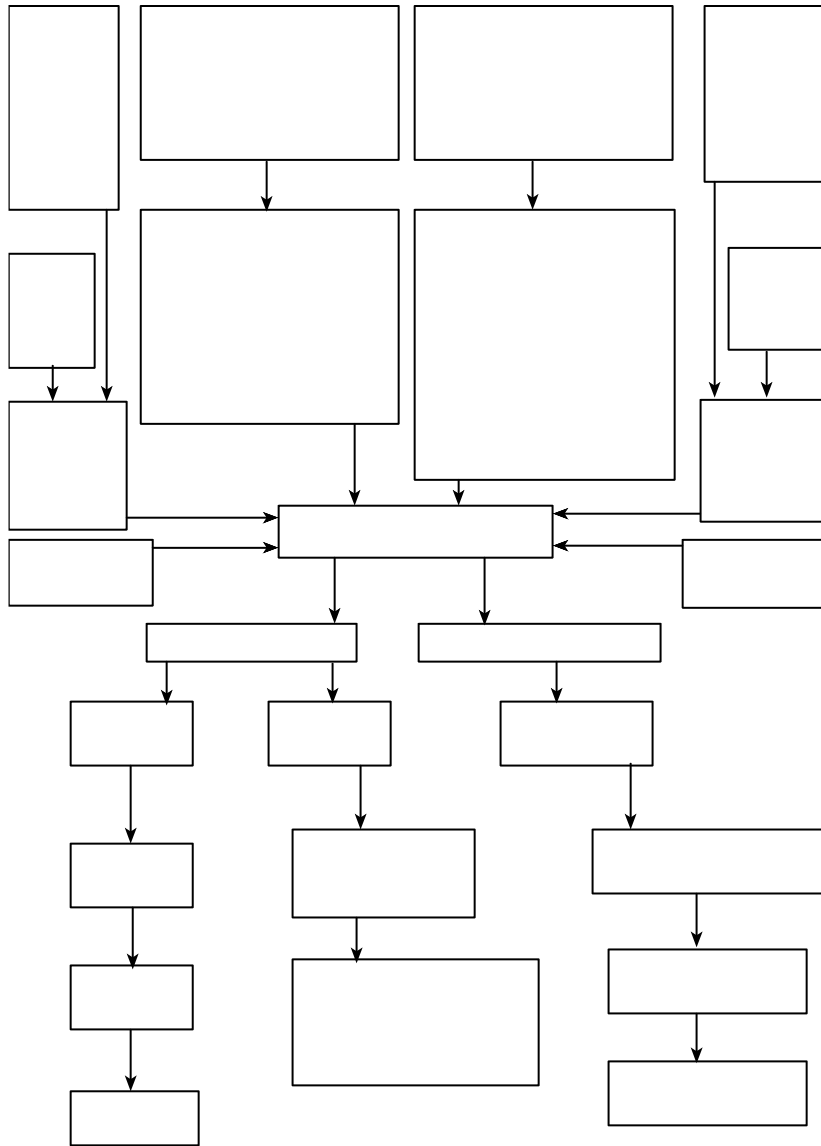
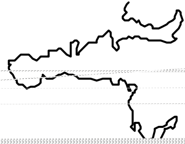


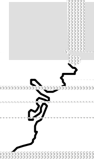
Fig. 1. The interaction between MNC and HC for a given investment proposal.

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





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 .0007 Tc-0.0007 Tw[(g

1,700 tons of solvents annually into the air. Volvo then decided against a paint shop and

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 tot he 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 occur 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 (locational 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

> 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.