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The impact of corporate and national cultures on decentralization in multinational corporations

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ABSTRACT

We develop and test a model of multinational corporation (MNC) decentralization in which the allocation of decision rights to subsidiaries is explained by aspects of both internal corporate culture as well as external national cultures. We extend the literature on MNC decentralization by testing the impact of both of these factors as determinants within the same model. Drawing on management control theory as a conceptual platform, we argue that the assignment of decision rights to a subsidiary in the MNC is impacted by corporate innovativeness and shared values, as well by aspects of home and host country cultures. We test our model on a sample of 119 MNC subsidiary managers drawn from a diverse range of industries and locations. The findings provide support to the proposition that corporate innovativeness positively impacts the decision to decentralize, whilst also indicating that home country individualism and host country uncertainty avoidance have a significant influence. The findings challenge established international management logic with respect to shared values—this variable is found to have a negative relationship with decentralization. Overall cultural distance is not found to be significant.

1. Introduction

We evaluate the extent to which corporate and national cultures influence decentralization to a subsidiary of a multinational corporation (MNC). Decentralization, or the allocation of decision rights to lower-level managers, is an important choice within a firm's management control system design (Abernethy, Bouwens, & van Lent, 2004). Prior research has shown how firm control systems are influenced by both firm-level characteristics and the external environment. For example, innovative firms are in general less centralized (Damanpour, 1991), MNCs may control their international subsidiaries through creating shared values in the organization (Nohria & Ghoshal, 1994), and a larger cultural difference between MNC home country and subsidiary host country is more likely to encourage a joint venture mode of entry (Kogut & Singh, 1988).

MNC decentralization has been studied extensively in the 1980s and early 1990s (Bartlett & Ghoshal, 1989; Gates & Egelhoff, 1986; Nohria & Ghoshal, 1994). Since that time, however, new challenges and opportunities in the global business environment have emerged. In many countries the entrepreneurial economy has replaced the managed economy, and new locations have emerged from which MNCs may source knowledge-based factors of production (Audretsch & Thurik, 2001). MNCs may now take advantage of global sourcing for innovation as well as cost-savings, developing and exploiting

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knowledge in countries such as India and China (Farrell, 2005; Levy, 2005). Changes in political regimes, regional integration, the forces of globalization and powerful developments in information and communication technologies (Archibugi & Iammarino, 2002) have also contributed to a need to reassess how MNCs organize and control themselves. Recent scholars have therefore, quite rightly, brought attention to decentralization and autonomy within MNCs as an important avenue of ongoing academic research (Paterson & Brock, 2002; Young & Tavares, 2004).

We propose and test a new model of MNC decentralization, one based on management control theory applied in an international context. We focus specifically on decentralization as a dependent variable, and argue that aspects of the internal corporate culture and the external national culture must both be taken into consideration when analyzing MNC decentralization. Corporate culture matters to organization decision making because it represents the system of ideals and beliefs in the organization; it is the "normative glue" that holds the organization together (Smircich, 1983, p. 344). National culture is also extremely relevant as managers' interpretation and responses to strategic issues differ according to their cultural characteristics (Schneider & de Meyer, 1991). There is little prior research that takes corporate and national culture into joint consideration when analyzing determinants of MNC decentralization (Young & Tavares, 2004).

We address this gap by focusing specifically on corporate innovativeness and shared values as indicators of corporate culture. In terms of national culture, we consider Hofstede's (1980, 1997) dimensions of national culture from both home and host country perspectives, as well as the overall cultural distance between home and host country (Kogut & Singh, 1988). Importantly, we use a research design where there is variation in both home and host country. This is a new approach that contributes to the MNC decentralization literature by testing the importance of both internal and external factors in the allocation of decision rights within modern day MNCs.

2. Theory and model development

2.1. Background to MNC decentralization

The strategy—structure paradigm that emerged in the 1950s and 1960s portrayed the large corporation as an organization whose structure, including its mechanisms of control, should follow its strategy (Chandler, 1962). When such large organizations internationalized, they transferred home country knowledge to overseas locations in pursuit of competitive advantage (Vernon, 1966). The headquarters was very much the main focus of analysis in this era, and decision-making seen to be more appropriate at higher levels in the organization (Clee & Sachtjen, 1964; Paterson & Brock, 2002). Since the 1980s, however, attention has shifted towards a more decentralized view of the MNC in which more decision-making rights are given to subsidiaries (Hedlund, 1993; Hedlund & Rolander, 1990). This emerging form allows for autonomy of work units, with authority emerging laterally (Stark, 1999). Subsidiaries came to be seen as more able to make decisions that influenced their own development (Morgan & Whitley, 2003; Young & Tavares, 2004). Thus there has been a shift in focus away from hierarchical views of the MNC, and from headquarters to subsidiary (Birkinshaw, 2001).

In this new paradigm, transnational management was deemed necessary for sustaining innovation and growth for the MNC (Ghoshal & Bartlett, 1990). Transnational management stressed an exploitation of global efficiency and an adaptation to local markets at the same time. This allowed foreign subsidiaries to be treated as unique organizations in their own right, even with their own strategies (Ghoshal & Bartlett, 1990; Jarillo & Martinez, 1990; Nohria & Ghoshal, 1994). In this view, overseas subsidiaries were not all controlled in a common, universal way (i.e., through centralization of decision-making in a headquarters), but through a differentiated approach whereby the most appropriate control mechanism (centralization, formalization, and/or socialization) depended on the nature and role of the subsidiary, in particular the complexity in its local environment coupled with the level of its resources and capabilities (Ghoshal & Nohria, 1997; Nohria & Ghoshal, 1994). Hence scholars highlighted an "increasing respect for autonomy" and linked national and regional strategies to higher economic rents for the MNC (Paterson & Brock, 2002). Young and Tavares (2004) undertook an extensive review of the literature on autonomy in organizations, with a particular focus on the MNC. These authors highlighted various factors that impact decentralization of decision-making into MNC subsidiaries. These include parent company factors (e.g., corporate culture and headquarter management style), subsidiary factors (e.g., age, size and range of functions), MNC strategy, embeddedness with external business networks, and the subsidiary role.

Young and Tavares (2004) also highlighted various outcomes of autonomy, including the innovative potential of subsidiaries, lateral communication and networked structures, and changes in mandate. In addition, autonomy can lead to local knowledge creation, thus allowing the so-called 'reverse' transfer of knowledge to the MNC headquarters (Ambos, Ambos, & Schlegelmilch, 2006; Gupta & Govindarajan, 2000). Reverse knowledge transfer into headquarters is important because such knowledge may embody details of subsidiary initiative or organizational practices that may be re-used elsewhere within the MNC (Birkinshaw, 1997; Jensen & Szulanski, 2004).

2.2. Management control theory

Management control is the process by which managers influence other members of the organization in such a way that their behavior will help in achieving the organization's goals (Anthony & Govindarajan, 2004; Merchant & Van der Stede, 2003). Elements of management control systems include budgeting, resource allocation, and performance measurement and reward. An important choice in the design of a firm's management control system is the level of decentralization: the extent