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Integration and responsiveness in subsidiaries in emerging economies

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ABSTRACT

The integration-responsiveness (IR) framework with the typology of international, multi-domestic, global and transnational MNE strategies has become a standard in international management textbooks. In particular, the 'transnational strategy' is advocated by some gurus, but considered unworkable by other scholars. Yet, despite the popularity of the framework, and the concept of 'transnational strategy' in particular, surprisingly little evidence exists for under which conditions this strategy is most appropriate. This paper revisits the typology using a contingency approach suggesting that the transnational strategy works well if it "fits" with other elements of a subsidiary's strategy. We test hypotheses derived from this perspective on a sample of subsidiaries in two emerging economies. We find that transnational strategy enhances subsidiary performance in particular if the subsidiary is wholly owned, if it was *not* established by acquisition, and if it is highly export oriented.

1. Introduction

The merits of standardization and localization of products and processes have been a pivotal theme in international strategic management research. A leading framework is the integration-responsiveness (IR) framework. Following Prahalad and Doz (1987), Bartlett and Ghoshal (1989) argue that local responsiveness and global integration can indeed be achieved simultaneously, and develop a typology based on a matrix of four strategies: international, multi-domestic, global and transnational. This typology has become a standard analytical tool in strategic management (e.g., Hill & Jones, 2013) and international business textbooks (e.g., Peng, 2014; Peng & Meyer, 2011).

Bartlett and Ghoshal recommend that multinational enterprises (MNEs) pursue a transnational strategy combining both global integration and local adaptation. Yet even companies they highlight as role models have since struggled, and have reverted to more 'global' organizational structures. Recent textbooks thus suggest that the 'transnational' strategy is rather idealistic and most firms have to make critical choices between global integration and local adaptation (e.g., Peng, 2014; Verbeke, 2013). However, solid empirical evidence regarding the merits of alternative types of strategy is surprisingly scarce. Few studies actually present solid evidence if and for whom either strategy would actually enhance subsidiary performance, as acknowledged by Ghoshal (1987) himself.

Our starting point for revisiting the Bartlett and Ghoshal typology is that the quest for generally applicable rules or performance effects may be futile because different strategies are effective for different types of subsidiaries. In particular, a transnational strategy combining global integration advantages with local responsiveness put high demands on the organization itself, such that it is not beneficial for every subsidiary. Therefore, a contingency framework is required to assess the merits of alternative strategies, and to identify under which conditions respectively global, multi-domestic and transnational strategies enhance subsidiary performance (Grewal, Chandrashekaran, & Dwyer, 2008; Katsikeas, Samiee, & Theodosiou, 2006; Roth, 1995). Hence, our research question is: *For which subsidiaries does a transnational strategy enhance subsidiary performance?*

Recent advances on knowledge management in MNEs emphasize the importance of knowledge exchanges and control mechanisms for different MNE strategies (Andersson, Forsgren, & Holm, 2002; Meyer, Mudambi, & Narula, 2011; Monteiro, Arvidsson, & Birkinshaw, 2008). The four types of strategy vary in the complexity of internal coordination and knowledge flows (Harzing, 2000; Pla-Barber, 2002; Wolf & Egelhoff, 2002). International strategies involve little explicit exploitation of either global integrating advantages or local adaptation advantages, and

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thus limited ongoing exchange of knowledge. Global strategies integrate strategic decisions and centralize core operations; knowledge flows thus are primarily top down, and control is tight. Multi-domestic strategies assign subsidiaries a specific scope with respect to local markets, but allow more local adaptation.

Transnational strategies create the most complex coordination challenges. They involve extensive intra-organizational trade, strategic coordination and knowledge exchange not only between headquarters and subsidiaries, but across subsidiaries in different countries. The different subsidiaries of the MNEs thus are highly interdependent both strategically and operationally (Harzing, 2000). To enable such complex coordination, the MNE needs not only formal structures but informal mechanisms (Foss, Husted, & Michailova, 2010; Tallman & Chacar, 2011). Bartlett and Ghoshal (1987, 1989) thus advocated the need for distinct organizational capabilities and a shared organizational culture that encourages cooperation and knowledge sharing. Extending this line of thought, we argue that a transnational strategy can have a positive effect on subsidiary performance if it 'fits' with other aspects of the subsidiary strategy.

The trade-offs between integration and responsiveness are particularly pertinent in countries with a distinct local business environment that inhibits the smooth transfer of business models. Especially in emerging economies, institutional frameworks often require idiosyncratic adaptations, while the local resource endowment is typically rich in labor but short of specialist human capital (Luo, 2003; Meyer & Peng, 2005; Xu & Meyer, 2013). In consequence, we expect a larger variation of strategies adopted by MNEs operating in such countries, and have thus chosen as our empirical field two emerging economies, Poland and Hungary. Our data are drawn from a questionnaire survey and include 345 observations of subsidiaries of MNEs. The dataset thus provides a rich variation of corporate strategy in a rapidly evolving context. Our results support our theoretical expectations that transnational strategies outperform other strategies if they fit with other aspects of the subsidiary strategy, specifically full ownership, establishment *not* by acquisition, and a high degree of export orientation.

This paper contributes to the literature in several ways. First, we develop a contingency perspective and offer empirical evidence on one of the most popular sets of concepts in the international strategy literature, transnational strategy, and the underlying the integration-responsiveness framework (Bartlett & Ghoshal, 1989), which to date suffers from a lack of empirical verification of its performance implications. Second, we offer new insights into subsidiary performance extending work on parent-subsidiary relationships (Birkinshaw & Morrison, 1995; Fang, Wade, Delios, & Beamish, 2013; Nell & Ambos, 2013; Tang & Rowe, 2012; Tian & Slocum, 2014) to show how strategy affects performance at the subsidiary level.

2. Conceptual Foundations

2.1. The integration responsiveness (IR) framework

In the 1980s and early 1990s, scholars began to systematically investigate the strategies of MNEs along the dimensions of local adaptation and global integration. Early studies tend to treat these dimensions as opposite poles of the same scale, or at as two highly correlated scales (Dow, 2006; Luo, 2001; Roth & Morrison, 1990; Venaik, Midgley, & Devinney, 2005). Prahalad and Doz (1987) challenge this approach suggesting that the two dimensions are not exclusive but can be combined if suitable organizational structures are created and implemented. They thus introduce the notion of a 'multi-focal' corporation that simultaneously is locally responsive and globally integrated.

These ideas are further developed by Bartlett and Ghoshal (1987, 1989), who develop the now famous 2×2 strategy matrix with the dimensions local responsiveness and globally integration, and identified four types of strategy. A global strategy focuses on global integration at the expense of local responsiveness, thus integrating organizational processes to a high degree and benefitting from economies of scale and scope as well as from integrated learning across a global organization. A multi-domestic strategy focuses on local responsiveness, for instance by offering locally adapted products in each market, yet foregoes potential economies of scale.[2] An international strategy, also known as home-replication strategy (Peng, 2014), is low on both global integration and local responsiveness. It thus benefits from neither economies of scale nor fit to local consumers, and thus is largely treated as an inferior strategy chosen only by MNEs with little international experience.

Bartlett and Ghoshal (1987, 1989) focus on the transnational strategy, which combines the benefits of global scale and learning with the benefits of locally adapted products and processes. It is associated with high levels of intra-MNE trade in goods and services, as well as extensive lateral knowledge flows. A transnational strategy also allows selected subsidiaries to become strategic centers for a particular product or technology (Harzing, 2000). It is thus associated with extensive knowledge flows not only vertically between headquarters and subsidiaries, but horizontally between different subsidiaries (Ghoshal & Bartlett, 1990; Gupta & Govindarajan, 2000; Kostova & Roth, 2003). In fact, every subsidiary is embedded in a different local community of practice, and the competitive advantage of the transnational MNE is to a large extend created by organizational learning that connect, integrates and exploits this geographically dispersed knowledge (Andersson et al., 2002; Chang, Gong, & Peng, 2012; Johnson, Arya, & Mirchandani, 2013; Meyer et al., 2011; Monteiro et al., 2008; Tallman & Chacar, 2011). Hence, subsidiaries are not only recipients of knowledge from the parent, but an important source of knowledge that contributes to the resource-base and the competitiveness of the MNE (Mahnke et al., 2005; Yang et al., 2008).

How do companies achieve integration and responsiveness simultaneously? Bartlett and Ghoshal (1987, 1989, 1993) suggest a combination of organizational capability, collaborative organizational culture and a matrix structure that facilitates intensive horizontal knowledge exchange within the organization. They present for example the cases of Ericsson (of Sweden) ABB (of Sweden and Switzerland) and Acer (of Taiwan), who at the time had adopted respectively a matrix-structure and a network structure of strategic and regional business units to achieve both high degrees of global coordination and responsiveness to local markets.

However, the transnational strategy – and especially the matrix organization needed to implement it – has been criticized as being overly ambitious, creating complex intra-organizational processes that create conflicts of interest, generate counterproductive organizational politics, and weaken incentives for individual business units (Midgely & Venaik, 2000; Chen, Chen, & Ku, 2012; Devinney et al., 2000; Foss, Husted, & Michailova, 2010; Mudambi, Pedersen, & Andersson, 2014). In fact, Ericsson, ABB and Acer went through periods of major strategic change when their strong organizational culture hit its limits in an organization of growing scope and complexity. We take this discussion forward by focusing on the interdependence of different elements of business strategy. Transnational strategy enhances subsidiary performance *only if* the complex coordination and knowledge management

[2] Bartlett and Ghoshal (1989) use the term 'multinational' for this strategy, but later authors adopted the term multi-domestic to avoid confusion with the concept of MNE, which encompasses firms pursuing any of these strategies.