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## Subsidiary knowledge creation in co-evolving contexts

Paul Ryan<sup>a,\*</sup>, Majella Giblin<sup>b</sup>, Ulf Andersson<sup>c,d</sup>, Johanna Clancy<sup>b</sup><sup>a</sup> School of Business, Trinity College Dublin, Dublin 2, Ireland<sup>b</sup> Department of Management, J.E. Cairnes School of Business & Economics, National University of Ireland, Galway, Ireland<sup>c</sup> School of Business, Society, and Engineering, Mälardalen University, Sweden<sup>d</sup> Department of Strategy and Entrepreneurship, BI Norwegian Business School, Box 883, 721 23 Västerås, Sweden

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## ABSTRACT

In this paper we explore how the MNE subsidiary's role internally within its corporation evolves through knowledge creation in accordance with an evolving external local knowledge network, and the extent to which the interwoven coevolving context matters for, and may be guided by the subsidiary. We conducted a qualitative investigation of purposely selected subsidiaries as case studies and longitudinally tracked the interwoven co-evolving contexts of their internal corporate role and external knowledge network. We show why role evolution may be differential and illustrate how competence-creating subsidiaries can balance and simultaneously manage the guided co-evolution of both contexts to advance their roles for knowledge creation. We develop a dynamic framework of subsidiary role evolution at the nexus of these interwoven co-evolving contexts. This advances theory on the dual embedded subsidiary as previous studies have predominantly been cross-sectional and static rather than evolutionary.

## 1. Introduction

Knowledge creation in the MNE is increasingly undertaken by foreign subsidiaries embedded in local networks (Andersson, Forsgren, & Holm, 2002; Birkinshaw & Hood, 2001). A subsidiary's ability to create knowledge in its local context emanates from its capacity to have a voice in its internal network and to evolve through a combination of local initiatives and corporate parental support (Cantwell & Mudambi, 2005). Its combinative capability (Almeida & Phene, 2004; Kogut & Zander, 1992) to manage knowledge both accumulated from within the MNE and absorbed from external sources is known to be critical to its knowledge creation capability (Phene & Almeida, 2008). It is at one and the same time dually embedded as part of its external local knowledge network and its internal MNE corporate network (Achcaoucaou, Miravitlles, & Leon-Darder, 2017; Ciabuschi, Holm, & Martin, 2014; Figueiredo, 2011). It can be argued that subsidiaries operate in these dual networks and aspire for self-preservation and typically advancement through the fusion of knowledge absorbed from its dual networks. It may therefore simultaneously seek to both advance its role within the corporate domain and draw resources and knowledge from a technologically advancing local domain. Essentially, it operates in a multiple set of contexts (Meyer, Mudambi, & Narula, 2011) each of which is continuously evolving, positively or negatively.

Several studies have examined either the evolution of a subsidiary's

role for knowledge creation in its internal context (Ambos, Andersson, & Birkinshaw, 2010; Asakawa, 2001; Birkinshaw, 1998; Birkinshaw & Ridderstråle, 1999; Dörrenbächer & Gammelgaard, 2010) or the evolution of the subsidiary's local knowledge network (Andersson, Björkman, & Forsgren, 2005; Boschma & Fornahl, 2011; Giblin & Ryan, 2012; Manning, Ricart, Rosatti Rique, & Lewin, 2010; Martin & Sunley, 2011; Menzel & Fornahl, 2009; Mudambi & Swift, 2012). However, how these evolutionary contexts for the subsidiary are interwoven and dynamic remains underexplored (Cantwell, 2014; Cantwell, Dunning, & Lundan, 2010; Michailova & Mustaffa, 2012). In this paper, we contribute to the shallow stream of co-evolution theory in IB research (Levin, Long, & Carroll, 1999; Lewin & Volberda, 2011; Madhok & Liu, 2006). In a qualitative study of heterogeneous subsidiaries based in a high-technology cluster, we show how knowledge creation for dual embedded subsidiaries occurs at the nexus of co-evolving contexts of internal MNE subsidiary role and local network knowledge base. For certain subsidiaries – dependent on the type of primary activity of the corporate company in terms of higher or lower order activities – these evolving contexts are proactively managed simultaneously leading to increased capability for knowledge creation.

The article is structured as follows: the next section of the paper develops the conceptual background. The article then outlines the methodology used to investigate the co-evolution of incumbent subsidiaries' roles and local network knowledge stock. The findings are

\* Corresponding author.

E-mail addresses: [paul.ryan@tcd.ie](mailto:paul.ryan@tcd.ie) (P. Ryan), [majella.giblin@nuigalway.ie](mailto:majella.giblin@nuigalway.ie) (M. Giblin), [ulf.r.andersson@mdh.se](mailto:ulf.r.andersson@mdh.se) (U. Andersson), [Johanna.clancy@nuigalway.ie](mailto:Johanna.clancy@nuigalway.ie) (J. Clancy).<https://doi.org/10.1016/j.ibusrev.2018.02.003>Received 10 February 2017; Received in revised form 6 February 2018; Accepted 10 February 2018  
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then presented. Discussion is provided and the contribution to theory from the case study is outlined. Finally, conclusions are drawn, limitations of our study presented and avenues for future research proposed in the last section of the paper.

## 2. Theoretical development

### 2.1. Subsidiary role evolution in the internal MNE network

Within the MNE, the subsidiary is embedded in a web of relationships with HQ and sister subsidiaries that can serve as a strategic resource for the subsidiary in its local network (Garcia-Pont, Canales, & Noboa, 2009). Relations with HQ determine the knowledge creation role for the subsidiary based on its charter (Birkinshaw, 1998). In the ideal scenario, the subsidiary's internal role evolves from its early existence as a passive recipient and executor of orders from HQ for mandated simple operation to, over several iterations, one as a creator and provider of critical knowledge for the entire MNE (Asakawa, 2001). However, very few subsidiaries arrive to this ultimate contributory role as a 'global innovator' (Figueiredo, 2011; Gupta & Govindarajan, 1991), 'centres of excellence' (Andersson & Forsgren, 2000; Holm & Pedersen, 2000). Ultimately, the subsidiary expands its knowledge creation role through initiative-taking (Birkinshaw, 1998; Birkinshaw & Ridderstråle, 1999). The initiatives are deployed to enhance the subsidiary's visibility and recognition through the attraction of attention in the MNE from HQ (Birkinshaw & Ridderstråle, 1999; Dörrenbächer & Gammelgaard, 2010). Taking initiatives can lead to increased recognition at HQ and also to increased monitoring (Ambos et al., 2010). A subsidiary may even dupe HQ and surreptitiously expand its knowledge creation role by covertly undertaking non-sanctioned initiatives. In essence, subsidiaries can be simultaneously attracting and avoiding HQ monitoring and attention in a complex power game of recognition and secrecy (Conroy & Collings, 2016). They sell initiatives and lobby HQ (Cantwell & Mudambi, 2005) and endeavour to align to HQ focal interests whilst protecting their own self-interests. There is this constant interplay between initiatives, autonomy, power and attention (Ambos et al., 2010).

During this evolutionary process, HQ and the subsidiary are in a perpetual bargaining process (Andersson, Forsgren, & Holm, 2007; Bouquet & Birkinshaw, 2008) where the subsidiary endeavours to influence HQ to expand its assigned role for knowledge creation. The bargaining takes place in the arena of contested resources within the MNE (Ambos et al., 2010). The achievement of, for example, a higher order mandate from HQ can mean that the subsidiary's status as a preferred partner in the local knowledge network is elevated. The MNE must protect as well as create valuable internal knowledge (Perri & Andersson, 2014; Perri, Andersson, Nell, & Santangelo, 2013; Shaver & Flyer, 2000) meaning that autonomy and control levels change over time (Asakawa, 2001). This iterative process, where the subsidiary takes initiatives and creates knowledge and resources in its local network to use in the bargaining process with HQ for an increased charter, and where the subsidiary utilizes its added mandate to further its potential knowledge creation in the local network, is a co-evolutionary process (McKelvey, 1997).

### 2.2. Evolution of knowledge stock in the external local network

In addition to a subsidiary benefiting from entering a local knowledge network, it may also, in turn, add to the dynamics of a local knowledge network. Pioneering subsidiaries can serve as catalysts for the creation of the local knowledge network (Giblin & Ryan, 2012; Manning, 2008), hence instigating its formation in the early stages of development. 'Flagship' subsidiaries (Rugman & D'Cruz, 2000) act as anchors in the local knowledge network (Feldman, 2003) that can educate and lobby government to take initiatives to deepen and diversify knowledge stock in the local network. They can also bring with them international quality standards, process and production knowhow

and knowledge on the extant international markets they serve, a global business model perspective and an international reputation in the marketplace (Giblin & Ryan, 2012). All this make them attractive partners to the indigenous businesses and start-ups who seeks to upgrade their knowledge and capabilities as well as to universities, research institutes, and government organizations on local, regional and national levels. The evolution of the subsidiary's role and knowledge development assignments from HQ is however intimately linked to the subsidiary's management of its dual contexts and its development of knowledge stock and quality. In this study we are first and foremost interested in illumining how knowledge creation in heterogeneous subsidiaries occurs within a co-evolutionary process of interdependent contexts, the MNE internal and the local external.

Local knowledge networks are attractive for MNEs insofar as they can access new knowledge by embedding operations in the local network (Andersson et al., 2005; Jenkins & Tallman, 2010). The local network consists of a set of actors interacting for knowledge creation and must be knowledge rich to be of value to incoming investors seeking to create knowledge. The relationships between actors in the network are both horizontal and vertical and create codified and tacit knowledge (Michailova & Mustaffa, 2012). Through these interactions the local knowledge network evolves and upgrades its knowledge base. An MNE subsidiary in such a local network is both a recipient and a source of knowledge in the upgraded local knowledge network. The subsidiary both influences and is influenced by the specific web of counterparts with which it interacts (Andersson et al., 2005; Cooke, 2004).

As a local knowledge network evolves it benefits from the learning associated with increased knowledge specialisation (Mudambi & Swift, 2012). Over time, however, the local knowledge network must develop multiple trajectories to ensure its longevity (Martin & Sunley, 2011). Over-specialisation and too inwardly focused local linkages can make it vulnerable to decline (Menzel & Fornahl, 2009) due to technological lock-in (Narula, 2002; Malmberg & Maskell, 2002) and a lack of capability to adapt quickly to technological disruptions. Local knowledge network resilience can be achieved through constant mutation, reorientation, renewal, or stabilisation (Martin & Sunley, 2011). The imperative for evolutionary growth of the local knowledge network is to expand its knowledge stock in terms of amount, quality, depth and breadth.

### 2.3. The co-evolving contexts for the dually embedded subsidiary

The MNE subsidiary therefore operates in a dual-network of local and global connectivity and membership (Meyer et al., 2011). There has been significant recent research on the situation of the MNE subsidiary at the nexus of its external local network and internal corporate network (Achcaoucaou, Miravittles, & Leon-Darder, 2014; Ciabuschi et al., 2014; Figueiredo, 2011; Meyer et al., 2011; Yamin & Andersson, 2011), which facilitates its knowledge creation within the MNE but also represents a formidable organisational challenge for the subsidiary (Birkinshaw & Pedersen, 2008). This is the case since there is a tension for the subsidiary between assuming or earning the autonomy to embed itself into and operate in the local knowledge network to create competencies, while still remaining integrated in the MNE. The dual context literature has however tended to take a static perspective on subsidiary activity in both networks, which neglects the dynamic nature of the process.

Corporate can have legitimate concerns about losing control over the subsidiary (Mudambi & Navarra, 2004). Another challenge for the subsidiary is to span its dual boundaries to achieve a position of optimal embeddedness so as not to be either under- or over-embedded in either network (Andersson et al., 2005; Garcia-Pont et al., 2009) and out of synch. From its bridgehead position between the corporate and local network (Ciabuschi et al., 2014) the subsidiary endeavours to gain a foothold in either its internal or external network or both that can serve

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