Topic: Strategy and structure of multi business and/or multinational firms

Sub-topic:

Determinants of subsidiary autonomy
Management summary

Which determinants are most evident on the issue of subsidiary autonomy? Multinational corporations (MNCs) should consider this question in order to be able to critically assess new investment options. The determinants that influence the level of subsidiary autonomy can be divided into 3 groups; MNC, subsidiary specific, and environmental factors. The objective of the MNC in regard of subsidiary autonomy is the maximization of profit and minimization of risk.

The first group of determinants can be derived from the MNC itself. These include; the stage of internationalization, the type of acquisition of the subsidiary, the diversification of the portfolio, the integration of the MNC network, the centralization vs. Decentralization, and finally the size and rate of growth of the MNC. Most of these factors are interdependent and can be used to set one general policy regarding subsidiary autonomy. However not every subsidiary can be treated the same therefore the subsidiary specific determinants have to be evaluated, these include; the role of the subsidiary for the MNC, the size of the subsidiary, the level of R&D, the level of external- and internal network integration, production of (not-) unique goods, the product life cycle, the local responsiveness, the power base of the subsidiary, and the top management. Finally we consider the environment subsidiary specific factors, these include; the degree of cultural distance, geographical distance, the stage of development of the host country, and the presence of scientific institutions. By using the latter two subsidiary specific groups of determinants, the MNC will be adept its general autonomy policy per individual subsidiary. All pre-mentioned determinants will be discussed in-depth in regard to subsidiary autonomy in this paper.

Future research could try to establish a clear link between the determinants; subsidiary size, subsidiary R&D, and subsidiary autonomy. Furthermore research should base itself upon research methods which can be generalized over the whole population and therefore should include time series evaluation to measure the direction of the level of subsidiary autonomy and the impact of the strategic decisions of the head quarters, in order to be better able to understand the impact of the determinants on subsidiary autonomy.
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Chapter 1; Introduction

1.1. Problem Identification
For many years now companies have ventured beyond the borders of their home country. This is done for good reasons like; expansion, risk diversification, opportunities, etc. CEO’s like to give their company the ‘brand’ of multi-national. This is because multinational corporations (MNCs) are perceived as more progressive, dynamic, focussed on the future, etc., than companies who operate solely in their domestic market (Perlmutter, 1996). MNCs operate thus in more than one market and/or country. Firms seek opportunities beyond their national border because this can result in additional economical benefits. MNCs can expand through several entry strategies e.g. exporting, licensing or franchising, alliances, joint ventures, acquisitions, etc. When an MNC enters a new market, the subsidiary in that market will have to grow quickly if it is to survive (Kendal & O’Donnel, 1996).

The possible growth of a firm is strongly related to the firm-specific managerial resources available (Vachani, 1999). Which are, as all resources are, limited. On top of this managers with inter-firm experience can only be gained incrementally through in-company experience. This means that firm growth in any given period is limited (Mahoney & Rajendran, 1992). In turn the autonomy an MNC grants its subsidiary is an important aspect when considering entering another market i.e. starting up a foreign subsidiary. This is because a subsidiary which needs a high degree of headquarters (HQ) control, consequently takes up a lot of managerial resources (Tan, 2009). This, as stated earlier, is a limited resource which cannot be bought. It is therefore important that when a company wants to acquire another company it takes into account how much control they think is needed in order to integrate that company successful into the MNC. Of course many other factors are important when entering another market e.g. the level of diversification of the portfolio of the MNC (Palich, et al., 2000). In this paper we will focus on how an MNC can determine which variables it should control for when determining the level of autonomy of a particular subsidiary. That is; which generalize-able factors influence the level of autonomy a foreign subsidiary is ideally granted from the MNC?

1.2. Problem statement
Hence the following question arises; which factors are expected to significantly affect the level of autonomy an MNC grants its subsidiaries, of course, to obtain the best possible results for the subsidiary but primarily for the MNC.
1.3. Research Questions

The first issue that is important when dealing with this problem is; how can subsidiary autonomy be defined? That is the extent to which an MNC grants its subsidiaries decision making autonomy in order to obtain optimal results.

Secondly, which inter-company factors are expected to have an influence on the level of autonomy a MNC gives its subsidiaries? In other words; to which extent can a MNC already determine the possible level of autonomy it has to grant its subsidiaries to obtain maximum levels of profit?

Thirdly, which intra-MNC factors, after acquiring / starting up the new subsidiary, are important when considering the level of autonomy is ideally required? This addresses the possible differences between the two companies and the influences this could have on the ideally required level of autonomy.

Furthermore it is important to consider the environment in which the MNC is expanding. Thus to what extent can a host country have an influence on the ideal level of autonomy a subsidiary requires?

Finally the three previous mentioned factors will be linked and evaluated in this paper. Other theories will also be considered in order to possibly improve decision making regarding the level of autonomy of a subsidiary.

1.4. Research method

Since we are interested in the factors that influence the decision making process of a MNC regarding the autonomy of its subsidiaries, a descriptive study will be necessary. Possible factors will be described as well as the possible relation of the factors to subsidiary autonomy. Most of the data used will thus be from secondary sources. These can be papers & articles, but possibly also general theories.

1.5. Relevance

In this paper all factors that, significantly, affect the level of autonomy an MNC grants its subsidiary will be evaluated. Possible new relationships will be drawn and/or new theories, when possible/relevant, will be connected to this issue. The relevance for an MNC could be that the decision process will be made easier and/or create a possible reduction in failures of newly acquired subsidiaries.
From an academic point of view this topic is relevant because findings in this paper could aid research for other papers, e.g. for empirical studies concerning this subject. Furthermore this research could identify one or more variables that should be controlled when conducting research to this topic, or any other relevant literature that should be incorporated. Moreover it could reveal links between factors regarding subsidiary autonomy which could result in making some variables obsolete, making it easier to predict/study optimal levels of subsidiary autonomy.

1.6. Overview

This paper has the following structure; in the second chapter the concept of subsidiary autonomy will be explored in depth. Also possible general areas that influence subsidiary autonomy will be defined. In the following chapters the general areas will be explored more in depth with possible new theories related to the area that is being discussed. In the last chapter the areas of influence will be linked together which will result in a conclusion, discussion and finally recommendations. Next to this, possible new topics for research will be identified in the last chapter.
2.1 **Relevance of subsidiaries**

The need to establish subsidiaries by MNCs became evident in the second half of the 20th century. As, for example, Rugman (1981) explains the significance of internal firm specific advantage (FSA) transfer within MNCs. Rugman (1981) emphasized the need to internalize external markets in cases where the business to business contacts lead to inefficiencies for the company and thereby negatively affecting the overall performance. This fact creates the need for companies to establish foreign affiliates which could exploit the FSAs for the company. Thereby generating higher profits than when products would have been sold or bought from or to another company. For example; when a company decides to expand to a new foreign market by acquiring another company, to serve the local market, that company has the need to control its new subsidiary (Nohria & Ghoshal, 1994). This is because what is best for the subsidiary (employment, production, and marketing) will not always be best for the company as a whole. This problem of goal incongruence will be explained in the next paragraph.

2.2 **Headquarters – subsidiary relations**

The relationship within the MNC between HQ and its subsidiaries can be seen as a principal – agent relationship. This relationship can be described by the Agency Theory (Eisenhardt, 1989). The agency problem describes the goal congruence problems that could occur since both, principal and agent are utility maximizers. Therefore agents will pursue their own interests which may conflict or diverge from the interests of the principal (Jensen & Meckling, 1976).

The Agency Theory is important to consider when, in a situation, there is a clear principal – agent structure. The HQ, being the principal, cannot make all the decisions within the MNC to achieve the highest possible result/utilization of the MNC FSAs. This is because of the fact that the MNC does not possess the unique knowledge a subsidiary has of the local market. However the HQ cannot give its subsidiary total freedom regarding all decisions that have to be made. Since the best interests of the subsidiary may not always be also in the best interest of the MNC as a whole (Nohria & Ghoshal, 1994). For this reason Intra-firm factors are considered in regard to subsidiary autonomy. Factors that increase the agency problem influence the level of autonomy that is deemed appropriate by a parent. Therefore the agency problem directly relates to the level of autonomy that is given by the headquarters to the subsidiary (Jensen & Meckling, 1976).
2.3 Subsidiary autonomy defined

A logical step forward for MNCs was to consider the level of autonomy their subsidiaries needed. Subsidiary autonomy can be defined as the degree of freedom a subsidiary gets from the MNC with regard to the decision making process on all levels that concern the subsidiary. Or in other words; All formal and informal rules and practices which have been developed over time in an organization in order to define a unit’s degree of discretion to control its own activities without interference from higher levels (Kallinikos, 1984).

Now that we have established what exactly subsidiary autonomy is and why an MNC more or less needs to grant its subsidiaries a certain level of autonomy, we can go on by considering what the dangers for the MNC could be when too little or too much control is exercised.

2.4 The level of subsidiary autonomy & possible consequences

Subsidiary autonomy is an important issue for an MNC since appropriate levels of control could result in significant benefits for the MNC and for the subsidiary. (Doz, 1986) From this fact it can be derived that subsidiaries can contribute to FSAs when proper control is applied. This has been validated by Brinkshaw et al. (1996). Porter (1992) argues that when incorporating a subsidiary into the MNC without giving it appropriate levels of control, it becomes over embedded in the MNC. Consequently this could cause the subsidiary to lose its credibility within the company and hereby it might miss out on future growth possibilities. On the other hand when too little control is exercised, i.e. too high autonomy, goal incongruence could occur. This often results in a less than optimal result for the MNC and possibly higher profits for the subsidiary (Roth & O’Donnel, 1996). Another reason for MNCs to consider the appropriate level of control a subsidiary needs at any one time is that they need firm specific managerial resources (Penrose, 1959). This can only be gained incrementally over time (Mahoney, 2005). Due to this reason firm specific managerial resources are thus a limitation on future growth of a firm which cannot be acquired / gained at will. Firms will therefore always try to use as little as possible firm specific managerial resources to control a subsidiary (Mahoney & Pandian, 1992). It is thus of great importance for an MNC to determine the proper level of autonomy it grants its subsidiaries since this greatly affects the MNC’s success in the short and long run.
### 2.5 Subsidiary autonomy divided

As the previous paragraph explains, subsidiary autonomy is an important factor for MNCs. A number of articles have addressed this issue identifying many factors that could influence subsidiary autonomy. In this section however general areas of influence will be identified and described. These will then in-turn be further explored in-depth in the forthcoming chapters.

The concept of subsidiary autonomy is one element of the structure of an organization. It is an instrument to reach an end. The end can basically be grouped in two basic elements; the maximization of profits and the minimization of risk. Decisions concerning subsidiary autonomy are thus basically based on profit maximization and risk minimization. The maximization of profits is an end of every organization. However for an MNC with foreign subsidiaries it is more difficult to control risk. Risk has different facets which differently affect the level of autonomy. Three main elements of risk are primarily important (Garnier, 1982).

The first element of risk is the importance of the subsidiary to the MNC and level of involvement of the MNC in the subsidiary. The greater this dependence the greater the tendency of the MNC will be to centralize decision making at the headquarters. Secondly the difference between the MNC’s home environment and the environment of the subsidiary is of influence of the risk involved. The larger these differences are the bigger the tendency will be to give the subsidiary more decision making autonomy. Finally the variability and unpredictability of the foreign environment bring a long-term additional risk. The greater this risk, the more important it is for a company to quickly respond to local changes, the more a MNC will thus be inclined to divert decision making autonomy to the subsidiary (Garnier, 1982). The firstly mentioned risk of dependence is general, and a consequence of having subsidiaries. The latter two types are to be considered for each subsidiary separately. The actual degree of autonomy will thus be determined by general policies, applicable for all, and by the characteristics of the individual subsidiary and the specific environment it operates in.

The subject of subsidiary autonomy can therefore be divided into three main categories, these categories being (Garnier, 1982):

1. *Intra-MNC determinants regarding subsidiary autonomy*; the outcome of this category will determine the general policy set by the MNC towards its subsidiaries.
2. *The specifics of the subsidiary;* using the subsidiary specifics the MNC will be able to determine whether or not deviations have to be made from the general set policy.

3. *The characteristics of the environment the subsidiary operates in;* this category gives the difference between the local environment and the subsidiary (foreign) environment, including the variability and unpredictability of that environment.

The following chapters cover these three categories which are based on the research of Garnier, (1982). He has also determined a number of elements for each category. However these will not be used since a lot on new research has been done since Garniers’ research.
Chapter 3; Intra-MNC determinants regarding subsidiary autonomy

Subsidiary autonomy is influenced by lots of different factors. In this section all intra-firm factors that influence the level of autonomy a subsidiary is generally granted by the MNC will be evaluated. Moreover we will look at the possibility for an MNC to set one general policy regarding subsidiaries by using the factors discussed in this chapter.

3.1 Internationalization of the MNC
Taggart & Hood (1999) found that the faster growing and more globally integrated an MNC is the less autonomy its subsidiaries enjoy. The level of autonomy can therefore be related to the stage of internationalization of the MNC. This finding is supported by Hedlund (1981). He found that in general subsidiary autonomy is less when the MNC has more international experience. In regard of this finding it can be concluded that the stage of internationalization and the level of MNC subsidiary autonomy are at least connected. When related to the four general types of strategies as described by Bartlett & Ghoshal (1988) this means that for the MNC with a global strategy a subsidiary will be integrated quickly in the MNC network and consequently will have low autonomy. Regarding the international strategy the subsidiaries, usually small distributors, will have higher levels of autonomy until they get bigger, when more control will be exercised, because of increased importance to the MNC. For the multinational strategy subsidiaries will relatively have more autonomy up to a higher point of interdependence due to the need for local timely responsiveness. The transnational strategy is linked to an early integration of its subsidiaries because of the high interdependence and coordination complexity which is inherent to such a strategy (Johnston & Menguc, 2007). The MNCs' level of internationalization is thus a general and easy way for a firm to start off in deciding what level of control is deemed necessary for a subsidiary.

The process of determining the level of autonomy should be for any firm an ongoing process. Nevertheless this process starts at the time when the new subsidiary is setup/acquired. In the next section the effect of the way the new subsidiary is incorporated into the MNC will be evaluated.

3.2 Type of acquisition
When an MNC is expanding through new foreign subsidiaries, the MNC can basically choose between two options; Greenfield investments and Acquisitions. Tan, D. (2009) explains that when interdependence within the MNC is weak and
uncomplicated, acquisitions are better since then also subsidiary-level firm-specific managerial resources are gained. In short acquisitions relieve HQ managerial constraint and consequently inherently will have more autonomy. That is; more autonomy then when a MNC starts up an entirely new company (Greenfield investment). The MNC will generally be better off doing a Greenfield investment when the interdependence within the MNC is strong and complex. If an MNC sets up a new company, this will generally require more firm-specific managerial resource than when another company would be acquired for obvious reasons. When an MNC fails to correctly apply these principles a lower growth of the subsidiary and consequently of the MNC will be the consequence (Tan, 2009). The interdependence of the MNC network is thus also an important determinant regarding subsidiary autonomy. This claim is supported by the work of Taggart & Hood (1999). They state that an acquired business has significantly more chance of having more autonomy then when a new company would be set up (Greenfield investment), unless the acquired plant is already part of another MNC. Moreover Young & Tavares (2004) also found supporting evidence that an acquired subsidiary enjoys more autonomy due to its past the subsidiary already has specific capabilities/relations which positively affect the level of autonomy. In short this means that when an MNC acquires an existing company, it will generally give that new subsidiary more autonomy then when the MNC would set up a new company. This effect is however moderated when the newly, already existing company, was already part of another MNC network. It has been also determined that the network interdependence is relevant in regard to the type of setup mode. This will be explored in-depth in section 3.3. When the MNC has decided upon the mode of set-up the role of the new subsidiary becomes important that the MNC has in mind. Therefore in the next section the effect of different roles of the subsidiary will be examined in regard to subsidiary autonomy.

3.3 MNC portfolio Diversification

The total global diversification of an MNCs’ portfolio has a significant effect on subsidiary autonomy. This effect is moderated by the MNCs’ organizational structure and stronger, i.e. greater autonomy, for marketing and personnel decisions then for R&D and finance decisions. Moreover subsidiary autonomy is lower when an MNC is diversified in related industries then when it is diversified in unrelated industries (Vachani, 1999). Therefore the level of portfolio diversification of an MNC is important when considering the appropriate level of subsidiary autonomy it should impose on its subsidiaries. That is because it was found that related diversification (product &
international geographic diversification, Vachani, 1999) leads to higher possible performance than unrelated diversification and when an MNC only targets a single market (Palich et al., 2000). Bearing in mind that firms in general will always want to maximize profits, they will most likely diversify their portfolio in related markets/industries. This is backed up by findings which concluded that 50% of the Fortune 500 companies in the 1980s reduced the level of unrelated diversification of their portfolio (Markides, 1995). From these findings it can be concluded that MNCs over the last years have the tendency to mainly diversify in related industries and that subsidiaries in related industries generally have/need less autonomy. Another factor that might influence subsidiary autonomy is the level of integration of the subsidiary in the MNCs’ network. In the next section, if possible, a link will be established.

3.4 Interdependence of the MNC network
As stated before the interdependence of subsidiaries within the MNCs’ network can be linked to the level of subsidiary autonomy. This directly relates to the level of integration of the subsidiary into the MNC network. The actual level of integration of a subsidiary into the MNC has also found to be a determinant for subsidiary autonomy; the more a subsidiary is integrated in the MNC the less the autonomy of the subsidiary will be and vice versa the opposite applies (Edwards et al., 2002; Taggart & Hood, 1999). This is supported by the findings of Garnier (1982) who concluded that when there is little interchange of products within the MNC, i.e. low integration, the subsidiary autonomy is positively affected, and vice versa again the opposite is true. Moreover the level of integration is can be related to the level of centralization vs. de-centralization of the MNC network. If an MNC has a decentralized operation, subsidiaries were tended to have higher levels of autonomy, however only regarding marketing and product strategy. On all other fields the autonomy was generally the same as with subsidiaries of MNCs whose operations could be described as centralized (Edwards et al., 2002). From this section we can conclude that the level of integration of the subsidiary into the MNC network is negatively related to its autonomy, and the degree of (de-) centralization of the MNC operations only affects subsidiary autonomy regarding marketing and product strategy. In the next section a possible relationship between subsidiary autonomy and the size of the MNC will be assessed.

3.5 Size & growth rate of the MNC
The sheer size of the MNC is also of influence on the autonomy a subsidiary is granted. For example; Garnier (1982) did find that if the MNC is relatively small, so in
comparison to a single subsidiary and absolute in comparison to other MNCs, the autonomy of its subsidiaries tends to be higher. Moreover if an MNC is experiencing a period of rapid expansion and fast growth, this will influence the degree to which the MNC will control its subsidiaries. Taggart & Hood (1999) concluded that when an MNC is going through a period of rapid expansion/growth this will negatively, i.e. reduce, the level of subsidiary autonomy that is granted by the MNC. This can be related to the level of internationalization of the MNC, see section 3.1.1 for further elaboration.

3.6 subsidiary ownership structure
The effect of ownership structure could have an effect on the level of subsidiary autonomy given by the MNC. It was discovered that the autonomy of a subsidiary is higher when still a large part of its common shares outstanding is held by local investors (Garnier, 1982). However this is only in the case when the shareholders are not widely disbursed which now a day usually is the case. Therefore it generally can be stated that the ownership structure is not of a significant influence on subsidiary autonomy. Besides, almost no literature has been written about it in the past two decades. Which would indicate the irrelevance of this subject or that it is not understood properly and consequently it is open for further investigation.

3.7 Conclusion
Considering all sections in this chapter it can be concluded that certain factors of an MNC significantly affect the ideal level of subsidiary autonomy. The most evident factors regarding subsidiary autonomy to be considered are; the MNCs' level of internationalization, the type of set-up/acquisition of the subsidiary, the MNCs' level of diversification of its portfolio, the level of subsidiary integration into the MNC network, whether the MNC has a (de-) centralized operation, and finally the size of the MNC. In the next chapter subsidiary autonomy will be evaluated purely from the subsidiaries perspective, i.e. which factors of the subsidiary do influence the autonomy it is generally granted.
Chapter 4; Subsidiary characteristics & autonomy

In this chapter the determinants regarding subsidiary autonomy will be evaluated purely from the subsidiaries point of view. Thus what characteristics of the subsidiary do influence the level of subsidiary autonomy? Each section explores a subsidiary specific factor in regard to subsidiary autonomy which has been deemed important by previous research.

4.1 Subsidiaries role, within the MNC

According to Gupta & Govindarajan (1991) there are four types of subsidiary roles divided according to two dimensions; knowledge inflow and knowledge outflow. The four types that can be distinguished are; the global innovator, which has a high outflow and a low inflow, the integrated player which has a high outflow and a high inflow, the implementor which has a low outflow and a high inflow, and the local innovator which has a low inflow and a low outflow of knowledge. The types have been validated and extended by Harzing & Noorderhaven (2006-1). The level of autonomy varies from low to high in the following order; implementors, integrated players, global innovators, and local innovators. In which thus the local innovators relatively enjoy the highest level of autonomy (Harzing & Noorderhaven, 2006-2). The specific role the MNC assigns to a subsidiary is thus of influence on the level of the autonomy of that particular subsidiary. However only the knowledge inflow and knowledge outflow have been considered, other subsidiary specific factors regarding the role of the subsidiary might play a role. These will be highlighted in the next section.

4.2 Type of subsidiary operation

MNCs determine, before they set up a subsidiary, what its purpose will be i.e. the type of operation the subsidiary is going to fulfill. The type of operations can be very diverse, in most cases it will however come down to a combination off; manufacturing, sales, marketing, R&D activities, etc. Each of these options will have, to some extent, an effect, positive or negative, on the level of autonomy. First of all when a subsidiary is granted higher levels of autonomy, this usually concerns marketing and product strategy (Edwards et al, 2002). However if a subsidiary manufactures goods which are also produced elsewhere within the MNC, the level of autonomy is significantly negatively affected, due to centralization (Simoes et al, 2002). On the contrary when a subsidiary produces unique goods, the level of autonomy has been found to be higher (Brinkshaw & Hood, 1997). What is more
when a subsidiary produces unique goods this usually is an indicator that the subsidiary has specific capabilities which will lever its position within the MNC, and therefore positively affecting the power it has and as a result the autonomy it enjoys. Nevertheless this is not the only possible explanation. A subsidiary may also enjoy more autonomy because it produces unique goods, however unique goods which are at the end of their product life cycle, and therefore not that important anymore to the MNC which also results in higher autonomy (Simoes et al., 2002). Moreover subsidiaries who are involved in high levels of R&D complexity usually enjoy more autonomy then when a subsidiary is only marginally involved in R&D activities (Taggart & Hood, 1999). Moreover a significant positive relation was established by Camison-Zornoza et al. (2004) between the size of a company and the level innovation, i.e. R&D activities. Furthermore subsidiaries that create more dependent and in-dependent relationships within and outside of the MNC network the better their position will be within the MNC innovative network (Andersson & Pahlberg, 1997). This again has a positive effect on the amount of R&D activities of the subsidiary which in turn positively affect subsidiary autonomy (Boehe, 2007). However it is argued that the R&D activities of a subsidiary need to exceed some basic level to be deemed important by the MNC, and consequently enjoy more autonomy (Simoes et al., 2002). Next we will on which market the subsidiary serves. When a subsidiary mainly serves the local market/economy, the subsidiary tends to have more autonomy (Garnier, 1982). This is supported by findings of Simoes et al, (2002). The main reason for this is that the subsidiary is, in this case, able to respond faster to changes in the environment of the local economy. Taggart & Hood (1999) also concluded that higher levels of autonomy could be related to a more locally responsive subsidiary (Taggart, 1998; Taggart & Hood, 1999). It has thus been established that subsidiaries who mainly serve the local market enjoy higher levels of autonomy and that subsidiaries who enjoy relatively high levels of autonomy are more often locally orientated. Moreover higher levels of export were also found to be of a positive effect on the level of autonomy (Taggart & Hood, 1999). Though, Simoes et al. (2002) found that the level of export activities, of a subsidiary, do not significantly affect the autonomy of the subsidiary.

To reiterate whenever a subsidiary produces unique goods, its autonomy will generally be higher and whenever it produces goods which are also produced elsewhere its autonomy will generally be lower. Also it can be stated that, above a minimum level, subsidiaries R&D activities can be positively related to its autonomy, and finally we can conclude that the level of local sales positively affects subsidiary autonomy and that the level of export does not influence subsidiary autonomy.
significantly. When a subsidiary is locally very active, to be competitive, the market thus demands local responsiveness.

4.3 Size of the subsidiary

Another, much researched, determinant is the size (absolute and relative to sister subsidiaries and the MNC) of the subsidiary effect on its autonomy. The bigger, relative and/or absolute, the subsidiary the higher the level of autonomy is (Hedlund, 1981; Simoes et al., 2002). Contradictory Taggart & Hood, (1999) found that size is negatively related to autonomy, i.e. the smaller the subsidiary the higher the autonomy. However the research of Johnston & Menguc (2007) might give an explanation. They concluded that at the relatively lower levels of the size of the subsidiary, subsidiary autonomy is positively related to the size of the subsidiary. This means that the bigger a subsidiary becomes the more autonomy it will generally enjoy. However this is true up to a certain point, after a certain point a negative relationship is evident between subsidiary size and autonomy. This means that the subsidiary size – autonomy relationship exhibits a quadratic inverted U shape. This can shortly be explained by the fact that the larger a subsidiary is the more resources it controls and the less the dependency upon HQ is (Hedlund, 1981). This increase in size will lead to a bigger interdependence with HQ and the other subsidiaries, hereby creating the need for HQ to exercise more control due to the subsidiaries increased importance to the entire MNC (Kumar & Seth, 1998). In general it can thus be said that the absolute and relative size of the subsidiary influence its autonomy. The pattern of this influence follows a quadratic inverted U shape, i.e. a small subsidiary has little autonomy, the bigger it gets the more autonomy it get up until a certain point where after the autonomy decreases

4.4 Subsidiary financial structure

The autonomy of a subsidiary is higher when still a large part of its common shares outstanding is held by local investors (Garnier, 1982). For further elaboration of how the financing of the subsidiary influences its autonomy please see section 3.5. In the next section the subsidiaries so called power base will be evaluated. This is the extent to which a subsidiary could have autonomy and which factors are necessary to be present at a subsidiary to actually make use of its specific capabilities to attain a higher level of autonomy.
4.5 Subsidiary power base

A subsidiary's relative power, i.e. control of critical resources and non-substitutability, as well influences its autonomy. The power, i.e. ability to influence the MNC on a strategic level, of a subsidiary is bigger when firms are highly internationalized and have a large share of their business and staff outside of the parent company (Forsgren & Pahlberg, 1992). There are 2 ways in which a subsidiary's power base can be evaluated; resource power and structural power. If a subsidiary controls critical resources it can use this to attain a higher level of autonomy. This is of course related to the dependence of the MNC on critical resources. The structural power refers to the position of the subsidiary in the network of the MNC. This determines the subsidiary's possibility to influence the MNC's strategic behaviour. Structural power is higher when a subsidiary is more involved in R&D activities, investment opportunities and the localization of new activities (Forsgren & Pahlberg, 1992). Furthermore Brinkshaw et al. (1998) found that when a subsidiary can use its internal resources in combination with initiative, that this greatly influences its contributory role to the MNC. Subsidiary initiative is strongly associated with leadership and an entrepreneurial culture of the subsidiary. The subsidiary contributory role is strongly related to the autonomy of the subsidiary. These findings apply under the limitation of a low competitive local market (Brinkshaw et al., 1998).

It can thus be concluded that when a subsidiary has the control of critical resources and has a good position within the MNC network, this positively affects the autonomy it might be able to obtain. However it is important that the subsidiary shows initiative, i.e. leadership & entrepreneurial culture, to actually make use of its control of critical resources and its position in the MNC network to obtain a higher level of autonomy.

4.6 Other subsidiary specific factors

Trust is an important factor in any relational context, thus also in a business environment. Therefore the frequency at which the top management of a subsidiary changes affects the credibility/trust outside parties and inter-firm parties have in the subsidiary (Simoes et al., 2002). Simoes et al. (2002) did find that when the top management of a subsidiary changed relatively often, this negatively affected the subsidiary autonomy. Another factor is whether or not the top management consists of locals or of expatriates. It was found that locally run subsidiaries have generally higher levels of autonomy than when the same subsidiary would be run by expatriates (Richards, 2000).
4.7 Conclusion

In this chapter the subsidiary specific factors regarding subsidiary autonomy are discussed. MNCs need to take subsidiary specific factors regarding the autonomy they grant a specific subsidiary, in order to maximize profits and minimize the inherent risk of owning a foreign subsidiary. The subsidiary specific factors that were deemed to have a significant effect on subsidiary autonomy are; the role of the subsidiary, the type of operations a subsidiary is engaged in and the extent of the specific operations, the relative size of the subsidiary, the responsiveness, and last but not least the utilization of the subsidiaries power base.
Chapter 5; The subsidiary environment & autonomy

The following determinants indicate the difference between local and home country environments (Garnier, 1982). These determinants are important for an MNC to consider when establishing a foreign subsidiary since these factors cannot directly be influenced. We will look at the following factors in regard to subsidiary autonomy; degree of cultural distance, the geographical distance, industry characteristics, and finally the host country characteristics and possible effort regarding subsidiary autonomy.

5.1 Degree of cultural distance
The degree of cultural distance and the level of autonomy a subsidiary is granted by the MNC is an often researched relation. The research of Wilkinson et al. (2008) summarizes the, in the past contradictory findings, i.e. the higher the cultural distance is; the lower the subsidiary autonomy (e.g. Root, 1987) vs. the higher the autonomy is (e.g. Kogut & Singh, 1988), and find a moderating variable. When an MNC enters a new (foreign) market cultural distance plays a role on the level of control HQ exerts over the subsidiary. However with the ageing of the subsidiary the cultural distance and its related height of control decreased to the point that it becomes insignificant. It can therefore be stated that cultural distance has only a temporary effect on the level of control HQ exerts over its subsidiaries (Wilkinson et al., 2008). It can thus be concluded that the level of control decreases as the subsidiary matures. Consequently the level of autonomy thus increases as the subsidiary matures. As a result, overtime, the variable of cultural distance becomes insignificant in regard to subsidiary autonomy. Next to cultural distance, geographical distance could be a factor of influence regarding subsidiary autonomy. This will be evaluated in the next section.

5.2 Geographical distance
The geographical distance between HQ and its subsidiaries has been found to be a factor regarding the role of the subsidiary for the MNC. When related to the four roles defined by Gupta & Govindarajan (1991), (see section 4.1 for an explanation), geographically isolated subsidiaries are more likely to be local innovators and less likely to be global innovators (Harzing & Noorderhaven, 2006-1). Since these roles were found to influence subsidiary autonomy (Harzing & Noorderhaven, 2006-2), geographical distance has a mediating effect on the type of role a subsidiary plays which in-turn affects the level of subsidiary autonomy.
5.3 Industry characteristics

In general the industry characteristics in which a subsidiary operates are of influence on the possibility of a subsidiary to attain autonomy and the possibility to influence the MNC on a strategic level (Forsgren & Pahlberg, 1992). When a foreign owned subsidiary operates in a ‘leading edge industry cluster’ (i.e. “an aggregation of competing and complementary firms that are located in relatively close geographical proximity” (Brinkshaw & Hood, 2000; 142)) it has stronger customer and supplier relations, and enjoys greater decision making authority than those not in such industry clusters (Brinkshaw & Hood, 2000). It is therefore important for countries to facilitate developments that encourage the creation of such ‘leading edge industry clusters’, and for subsidiaries it is of value regarding the level of their autonomy. In the next section host country factors that influence subsidiary autonomy will be evaluated as well as it will be evaluated whether or not it is beneficial for a host country to have subsidiaries who enjoy more autonomy or not and what a host country can do to influence the level of autonomy attained by foreign subsidiaries.

5.4 Host country factors

Taggart, (1999) claims that the higher the autonomy of a subsidiary is the higher the development potential for the host countries economy is, this is supported by findings of Edwards et al. (2002). Furthermore subsidiary autonomy is also related to the level of the host country development (Katrin et al., 2005). The more developed the host country is the better the infrastructure is, the education & skills of the work force, and other public goods. These are positively related to autonomy because of the higher possibility of the subsidiary to be more embedded in external networks (Young & Tavares, 2004). Moreover Ghoshal & Bartlett (1988) found that higher levels of subsidiary autonomy facilitate locally developed innovations and the diffusion of these innovations throughout the MNC. In addition they did conclude that higher levels of autonomy do not negatively influence the adoption process of MNC innovations in the subsidiary. It can thus be stated that R&D activities in a subsidiary will equally good be adopted by the entire MNC as R&D activities from HQ. Therefore the MNC will not hesitate to locate R&D activities to its subsidiaries. However on the contrary Katrin et al. (2005) concluded that higher subsidiary autonomy does not imply a higher positive impact on the local economy, they state that it is more beneficial for the local economy that subsidiary is developing.

Rugman & Douglas, (1996) state that 3 conditions should be fulfilled in order for a host country to fully benefit from the operation of the subsidiary. Firstly, downstream innovation (i.e. knowledge inflow from the MNC to the subsidiary), which results in a
high value added component that is positive for the host countries export. Secondly, new product lines which usually result in R&D activities in the host country, and finally the global responsibility for marketing the product lines that the subsidiary produces, i.e. Global Mandate. Whereas the first condition has not been found to significantly affect autonomy (Simoes et al., 2002), and the latter have been positively related to autonomy (Boehe, 2007; Source). Moreover Davis & Meyer (2004) identified 4 areas, for host countries, that maybe important to subsidiary R&D, which is of influence on the subsidiaries autonomy. Namely; local competitive conditions, local supply conditions, access to scientific institutions, and host government support. All of which can be directly or indirectly influenced by the local government. They discovered that only the access to scientific institutions has a positive relation to the incidence en level of R&D conducted by companies in general. Furthermore they concluded that host government support is important in encouraging the incidence of R&D but it does not lead to higher levels of R&D (Davis & Meyer, 2004). To conclude contradictory findings exist regarding whether it is beneficial for a host country to have foreign owned subsidiaries who have more autonomy. A relationship was established between the development of subsidiaries and the benefits for the host country, and the most important measure a host country can take to influence subsidiary autonomy is to facilitate in the development of ‘leading edge industry clusters’ and the access to scientific institutions.

5.5 Conclusion
From this chapter it can thus be settled that the cultural distance has a significant effect in the earlier stages of the ‘age’ of the subsidiary, but that after some time this factor becomes neglect-able. The geographical distance has only found to be of an issue on the role of the subsidiary when a subsidiary is geographically isolated from the HQ and from sister subsidiaries. Whereas the industry characteristics influence subsidiary autonomy when so called ‘leading edge industry clusters’ exist. Finally the host country can influence subsidiary autonomy thru; infrastructure, highly educated/skilled workforce, and access to scientific institutions.
From the conclusions and information obtained in the last three chapters the following framework can be drawn:

### Figure 1
Factors affecting subsidiary autonomy

<table>
<thead>
<tr>
<th>Intra- MNC determinants</th>
<th>Subsidiary Specific Characteristics</th>
</tr>
</thead>
<tbody>
<tr>
<td>- Stage of Internationalization +/-</td>
<td>- Specific role of subsidiary +/-</td>
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<tr>
<td>- Integrations of the MNC network +/-</td>
<td></td>
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<tr>
<td>- Centralization / Decent +/-</td>
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<tr>
<td>- Type of set-up +/-</td>
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<tr>
<td>- MNC growth rate +/-</td>
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<tr>
<td>- Size of the MNC +/-</td>
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<tr>
<td>- Portfolio diversification +/-</td>
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<tr>
<td>- Specific role of subsidiary +/-</td>
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<tr>
<td>- Local responsiveness +/-</td>
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<tr>
<td>- Structural &amp; resource power +/-</td>
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<tr>
<td>- (in-) dependent relationships +/-</td>
<td></td>
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<tr>
<td>- Manufacturing (not-) unique goods +/-</td>
<td></td>
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<tr>
<td>- Expatriate top management +</td>
<td></td>
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<tr>
<td>- Local top management -</td>
<td></td>
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<tr>
<td>- Rotation of top management +/-</td>
<td></td>
</tr>
</tbody>
</table>

Subsidiary initiative +/-

Cultural distance & age subsidiary +/-
Geographic distance & isolation +
Leading edge industry clusters +/-
Scientific institutions +/-

Subsidiary specific environment
Chapter 6; Conclusions, discussion, and recommendations

6.1 Conclusion
The factors that are foremost in determining the autonomy of a subsidiary are; The stage of globalization of the MNC, the type of acquisition of the subsidiary, the portfolio of the MNC, the level of integration of the subsidiary into the MNC network, the level of centralization vs. decentralization, the absolute size of the MNC, and the rate of growth of the MNC. These determinants are derived from the MNC and will be the basis to set one general policy regarding subsidiary autonomy. What also can be stated is that all these factors influence each other. For example this comes down that a subsidiary which is part of a global MNC consequently with a high integration into the MNC, a high degree of MNC centralization, high internal dependence, and a low need for local responsiveness, will not have high autonomy.

The following factors are subsidiary specific; The role of the subsidiary, the (in-) dependent relationships the subsidiary has, the size of the subsidiary, the level of R&D, the type of goods the subsidiary produces, and whether the subsidiary serves the local market or not, the stability of the top management in term of personnel, and the top management has to exist mainly out of local employees. However to actually use these subsidiary specific factors to attain higher levels of autonomy the following factor needs to be fulfilled; the Management has to show initiative, i.e. good leadership and an entrepreneurial culture.

Finally the environment of the subsidiary is situated in is of impact on the subsidiary autonomy. The following factors are of influence; The cultural distance which becomes insignificant after the maturing of the subsidiary, the geographical distance which only has to be accounted for when the subsidiary is isolated from the MNC and other sister subsidiaries, the existence of scientific institutions, and lastly the stage of development of the host country.

Some contradictory and unclear findings were evident in the literature that was consulted; these will be discussed in the nest section.

6.2 Discussion
The first question mark that one can put with almost all the empirical studies consulted in this literature review, is whether the studies can be generalized. Most studies have used companies from only one to at most six countries. Moreover the studies were generally from one moment in time. Some; like Taggart & Hood (1999) try to overcome this by using the ‘5 years ago / in time’ method. Nonetheless these methods are likely to contain bias. The following contradictory findings were evident;
The size of the subsidiary in regard to the autonomy shows a quadratic inverted U shape. Furthermore the size of the subsidiary is positively related to the level of R&D in the subsidiary. These two findings contradict since the level of R&D is positively related to the level of subsidiary autonomy. This indicates that the level of R&D at some point would also start to show a quadratic inverted U shape or that the level of autonomy would as well show a purely positive relation to the size of the subsidiary. It is also argued that subsidiary initiative is important to actually make use of the resources of the subsidiary to attain a higher level of autonomy.

6.3 Recommendations

To control for the biases that have been present in the literature a better, but more costly and time consuming, method to measure subsidiary autonomy could be to measure subsidiary autonomy over multiple points in time (time series), and both from the HQ and subsidiary perspective, in a sample among many countries (where the HQ is based). To assure that the findings can be applied in any study. Moreover further empirical research is needed when it comes to the two factors subsidiary size and the level of subsidiary R&D in relation to subsidiary autonomy. The link between these variable should be investigated from all possible angles. So the link between; subsidiary size and R&D, subsidiary R&D and size, subsidiary size and R&D in relation to subsidiary autonomy, subsidiary autonomy and size in relation to R&D, and finally subsidiary autonomy and R&D in relation to size. While controlling of course for all other variable mentioned in this paper. This will help MNC to understand the relationship between these variable, this can help MNCs to grant subsidiaries better levels of autonomy which should have a positive impact on the overall profit of the MNC.
References:


