



Control mechanisms of MNEs and absorption of foreign technology in cross-border acquisitions[☆]



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ABSTRACT

This study investigates the impact of control mechanisms exercised by MNEs on knowledge (technology) absorption in cross-border acquisitions (CBAs). The empirical examination was undertaken in Korea, which is a newly industrialized emerging market, where knowledge acquisition from foreign investing firms is particularly important to leapfrog into advanced economies. We find that most of the control mechanisms (i.e., 'staffing the top management positions', 'participation in the policy making and planning process', 'interaction of the subsidiary's top management with the MNE' and 'participation of foreign expatriates in key functional areas') have a positive association with organizational learning. In addition, we also uncover that *provision of training programs* for a fixed period creates more synergy when it is combined with constant and continuous education in daily activities. This study contributes significantly to the body of control mechanism literature and the understanding of CBAs, and also provides practical implications for MNEs intending to enter foreign markets by partially purchasing the equity shares of local firms.

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1. Introduction

Park, Glaister, and Oh (2009) describe cross-border acquisitions (CBAs) as strategic investments carried out by multinational enterprises (MNEs) in order to overcome the competitive pressure for globalization and improve their position in the world market. They consider CBAs where the MNEs make a partial equity purchase of the local firms. These CBAs are therefore a hybrid organizational form which requires a cooperative business relationship between acquiring MNEs and acquired local firms, whose headquarters are located in different countries. CBAs are currently one of the most popular forms of investment worldwide and represent a critical alternative for strategic expansion (Shimizu, Hitt, Vaidyanath, & Pisano, 2004). Based on contemporary movements, acquisitions have replaced Greenfield investments as the most common mode of foreign investments (Ivarsson & Vahlne, 2002).

There may be various reasons for their prevalence. Shimizu et al. (2004) point out that a major element playing a pivotal role in contributing to the popularity of CBAs is: 'rapid changes in technical standards' promoted by globalization and the consolidations of industries and regions. According to Apfelthaler, Muller, and Rehder (2002), firms are surrounded by an increasingly competitive, complex and uncertain environment. In this situation, CBAs are unique arrangements helping firms develop competitive advantage by improving organizational efficiency and effectiveness. Hitt, Harrison, Ireland, and Best (1998) shed light on the fundamental character of CBAs by illustrating their formation as a vehicle to blend

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complementary capabilities of MNEs and local firms. These explanations have a trait in common, the emphasis on the importance of organizational knowledge (as a complementary resource), in that a firm's competence cannot be enhanced without the enlargement of the organizational knowledge reservoir. The possession of distinctive technology and information is a key competitive advantage. In this vein, [Park and Ghauri \(2011\)](#) suggest that the most significant strength of CBAs resides in the fact that both foreign and local firms have the opportunity to learn complementary skills and know-how through the establishment.

However, CBAs are complicated and multi-faceted events and thus they often fail to achieve their initial investment objectives. Among the more common reasons for failure, MNEs may choose an incorrect target, pay too much or inadequately integrate it ([Hayward, 2002](#)). Although these are crucial grounds for unsuccessful operations, we also should not overlook the links between organizational performance and foreign control mechanisms. To reiterate, MNEs undertake strategic investments to break into and defend their foreign markets, and subsequently maintain a better position in their international operations. MNEs possessing partial ownership in CBAs commonly attempt to exert an adequate level of control to make their achievement of organizational goals more predictable ([Li, 2003](#)) and use special methods (i.e., control mechanisms) to ensure that the subsidiaries are managed to meet their strategic interests ([Hebert, 1996](#)). They influence managerial and operational decisions of the subsidiaries through the use of power, authority and a wide range of bureaucratic, cultural and informal mechanisms. These various control mechanisms eventually function as a prime mover to transfer sophisticated foreign knowledge and advanced MNE technology ([Park, 2009](#)). The appropriate exercise of control mechanisms is thus a critical prerequisite determining the efficient operation of overseas subsidiaries and guaranteeing a triumph in the competitive learning race against other local competitors and a crucial component comprising the part of absorptive capacity in learning organizations. However, this issue (i.e., the association between control mechanisms and subsidiary knowledge absorption) seems to have remained as a big gap in current academic discussions.

In addition to the lack of empirical experiments on the above, some other gaps are also noticeable. For instance, despite the recent prevalence of CBAs and the general consensus on the importance of acquisition of technological information by subsidiaries, vast scholarly concentration has been paid to 'knowledge acquisition by international joint ventures (IJVs)' (e.g., [Anh, Baughn, Hang, & Neupert, 2006](#); [Lane, Salk, & Lyles, 2001](#); [Lyles & Salk, 1996](#); [Park, 2011](#)), but learning in CBAs has received scant attention. In fact, although in-depth examination of knowledge exchange between foreign and local firms in the same entities (i.e., CBAs) has been proceeding (e.g., [Håkanson, 1995](#); [Hayward, 2002](#); [Ivarsson & Vahlne, 2002](#); [Zou & Ghauri, 2008](#), among others), a thorough review of the literature using EBSCO, Elsevier ScienceDirect and Proquest indicates that such empirical studies are focused only from an MNE perspective. However, knowledge exchange is not a unilateral but a bidirectional phenomenon, which points out that we need to approach this issue from different angles (i.e., knowledge acquisition from investing firms by local firms). In addition, empirical examinations attempting to identify key factors affecting knowledge exchange between MNEs and subsidiaries have been primarily carried out in transitional economies such as Hungary, Vietnam and China and neglected emerging countries (e.g., [Anh et al., 2006](#); [Lane et al., 2001](#); [Lyles & Salk, 1996](#); [Tsang, 2002](#)).

Korea is especially suitable to examine the topic in that it has long been regarded as an emerging economy which has attracted huge foreign investments, and thus control mechanisms exercised by foreign firms and its impacts have also been considered to be important for MNE operations. The country is often referred to as one of the East Asian tigers (i.e., Hong Kong, Taiwan, Singapore and Korea) which achieved very rapid economic growth up until 1997. These so-called Asian tigers grew twice as fast as other Asian countries, three times as fast as Central and South American countries and five times as fast as sub-Saharan countries in Africa ([Ahn, 2001](#)). Among these Asian tigers, Korea is the best example, showing interrelations between significant changes in FDI policy, the enlargement of the volume of attracted FDI, the rise of CBAs and an increased role of knowledge acquisition in recent years. In particular, the Asia crisis in 1997 triggered changes in the government attitude toward foreign investments, and subsequent enhancement of the business environment through aggressive FDI liberalization strategies enabled Korea to attract a dramatic increase in foreign investment resulting in the sharp surge in equity purchases by MNEs of local firms ([Jeon & Ahn, 2004](#)). Moreover, knowledge acquisition is a crucial issue for the Korean economy in order to leap forward and establish itself as an advanced economy. These explanations clearly propose that Korea is an important research context when a single geographical area is chosen to explore the phenomenon.

In conclusion, although acquisition of complementary knowledge is one of the central motivations for two entities to form CBAs (i.e., MNEs and local firms), it has generally received scant attention in the extant literature dealing with the research topic. Of course, there are some welcome exceptions, however, to the best of our knowledge, previous studies have focused only on the MNE perspective and neglected opposing angles in the phenomenon (as discussed, knowledge acquisition between MNEs and CBAs is bidirectional). In addition, no one has attempted to identify the impacts of foreign control mechanisms on knowledge acquisition in CBAs despite their strategic importance particularly in the emerging economy context. We will try to fill these research gaps. Based on the discussion, the aim of this research is to identify foreign control mechanisms positively influencing CBA knowledge acquisition from MNEs in the perspective of Korean local firms.

2. Research model and hypotheses development

Control mechanisms can be classified into two different types: management and operational. Management control "is the observable pattern of decision-making power. Although ownership control may lead to management control ... through board membership, other more informal control mechanisms ... may provide decision-making power apart from that which

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